BLEED THROUGH POOR COPY

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 284—October Term, 1953.

(Submitted June 22, 1954 Decided January 11, 1955.)

Docket No. 22426

JOSEPH A. PHELAN,

Complainant,

—v.—

MIDDLE STATES OIL CORPORATION, *et al.*,

Defendants.

MEYER KRAUSHAAR and SOPHIE D. COHEN, as executors of William W. Cohen, deceased, SOPHIE D. COHEN, individually, and LEVY BROTHERS,

Appellants,

—v.—

JOSEPH GLASS and JOSEPH P. TUMULTY, JR., executor of Joseph P. Tumulty, receivers, and MIDDLE STATES PETROLEUM CORPORATION,

Appellees.

Before:

L. HAND, SWAN and FRANK,

Circuit Judges.

2017

Appeal by Meyer Kraushaar and Sophie D. Cohen, as executors of William W. Cohen, by Sophie D. Cohen, individually, and by Levy Brothers, from a judgment of the United States District Court for the Southern District of New York (Joseph J. Smith, *J.*, presiding), overruling objections to the application of Joseph Glass and Joseph P. Tumulty, for a discharge, as receivers of United Oil Producers Corporation, granting them such a discharge, and dismissing a claim against Middle States Petroleum Corporation.* Joseph P. Tumulty died pending the appeal and Joseph P. Tumulty, Jr., his executor, has been substituted in his place.

MEYER KRAUSHAAR *for the appellants.*
LESLIE KIRSCH *for Glass.*
RALPH MONTGOMERY ARKUSH *for the Middle States Petroleum Corporation.*
JOSEPH P. TUMULTY, JR. *pro se.*

L. HAND, *Circuit Judge*:

We dismissed an appeal from the judgment in this case because it was not final against Glass, and because, although it was so against Tumulty and the Middle States Petroleum Corporation, it would have resulted in great duplication of time and expense to go over the same issues twice. We suggested then that the parties might stipulate to delete those parts of the judgment that limited its finality as to Glass and to discharge him unconditionally.** This they did, but in two other opinions, on January 15 and February 8, 1954,† we concluded that such amendments

---

* 124 Fed. Supp. 728.

** *Phelan* v. *Middle States Oil Corporation*, 203 Fed. (2) 836.

† *Phelan* v. *Middle States Oil Corporation*, 210 Fed. (2) 360.

BLEED THROUGH POOR COPY

must be approved by the district court under Rule 23 (e); and we therefore remitted the cause to Judge Smith. On May 21, 1954, after hearing on notice to all parties he entered a judgment amending the judgment, from which, as amended, the original appellants have again appealed. The present judgment (disregarding the reversal of the dismissal of the counterclaim of the Middle States Petroleum Corporation against the executors of Cohen) now unconditionally declares (1) that Cohen's executors, and Levy Brothers and Sophie D. Cohen individually "have failed to establish any right to surcharge against Joseph P. Tumulty and Joseph Glass, as Receivers of the United Oil Producers Corporation, or recovery against Middle States Petroleum Corporation in favor of the estate of United Oil Producers Corporation or any of those claiming through said estate"; (2) denies all motions to surcharge the receivers and approves their accounts; (3) discharges them as such receivers; (4) dismisses the "general charges of fraud and conspiracy"; and (5) dismisses nine "specific claims of fraud and conspiracy" which it describes severally in detail. The judgment leaves undisposed of all liabilities of Glass and Tumulty, as receivers of the Middle States Oil Corporation, or of any of its 35 and more subsidiaries. We need not decide many of the issues litigated at the trial, even though these related to the rights and liabilities of the United Oil Producers Corporation against, or to Middle States Oil Corporation, or any of its subsidiaries, save as decisions on these bear upon the value of the assets of United Oil Producers Corporation, sold in reorganization. Ordinarily, of course, it would be necessary to liquidate these claims as to both their validity and amount in order to appraise their value, and to decide whether the price at which they were sold to the Middle States Petroleum Corporation was "fair." However, as we shall show, it is not necessary to do this in the case at bar because the

intercorporate claims were complicated far beyond any possible liquidation within the time allowed by the district court for that purpose. The only question is whether the price fixed and obtained was the best attainable in the circumstances. If it was, that was all for which the appellants can now demand the receivers of the United Oil Producers Corporation to account. For these reasons we shall not discuss any claims of Cohen's executors, as shareholders of the Southern States Oil Corporation, or the claims of Sophie D. Cohen, individually, or of Levy Brothers, as such shareholders. These have no bearing upon the liability of Glass and Tumulty to the bondholders or creditors of United Oil Producers Corporation. Nor has the claim of Sophie D. Cohen, as a shareholder of the Oil Lease Development Company, any such bearing, because, even though we will assume for argument that she may have been entitled to prosecute the claims of that company, its only claim against the receivers of United Oil Producers Corporation, was as a pledgee of some of the bonds of that company, so that whatever disposes of the interest of Cohen's executors, as holders of such bonds, applies equally to the interest of Sophie D. Cohen, as shareholder of Oil Lease Development Company.

We shall use the following abbreviations: The "Bondholders" will mean all those bondholders who did not deposit their bonds in reorganization; "U.O.P." will mean United Oil Producers Corporation; "M.S.O." will mean Middle States Oil Corporation; "M.S.P." will mean Middle States Petroleum Corporation; the "Receivers" will mean Glass and Tumulty, as receivers of United Oil Producers Corporation. The appeal involves only three questions: (1) Whether the sale to "M.S.P." in reorganization of the assets of "U.O.P." was conducted as the law requires; (2) whether the plan of reorganization satisfied the Boyd

BLEED THROUGH POOR COPY

Rule* by giving to bondholders an "equitable equivalent" in "M.S.P." of their former claims against "U.O.P."; and (3) how far the "Receivers" are liable personally if either answer to the foregoing questions is negative. The claim against "M.S.P." is that, as it was a party to the sale and to the consequent plan of reorganization, it was a grantee of a fraudulent conveyance. The charge against Glass rests more particularly upon the allegation that he actively promoted the reorganization fraudulently as part of a conspiracy to secure an interest for himself in "M.S.P."; and that, even if not a party to any such actual fraud or conspiracy, he had such personal interests in transferring the assets of "U.O.P." to "M.S.P." as conflicted with his duty as receiver, and threw upon him the burden of justifying his conduct, a burden which he did not carry. Furthermore, the "Bondholders" charge that, even though Glass was not engaged in a conspiracy to defraud them, the "Receivers" were derelict in their duty as such, in the conduct of the sale of the assets, and that the burden of proof lay upon them to show the extent of the loss incurred and their profits therefrom.

After a long and warmly contested trial, Judge Smith handed down a comprehensive opinion, accompanied by 272 findings of fact, in which he decided that the "Bondholders" had failed to establish any liability against the "Receivers" or "M.S.P."; but which dismissed the counterclaim of "M.S.P." against Cohen's executors. To the allegation that Glass and the committee that reorganized "M.S.P." united in a conspiracy to secure the assets of "U.O.P." in fraud of the "Bondholders," Judge Smith found that the "general charges of fraud and conspiracy are not proved." Of Glass he said that "he gave the impression, during his extended testimony, of sincerity and

---

* *Northern Pacific Railway* v. *Boyd*, 228 U. S. 482.

honesty of purpose. He was unconvincing on two subjects—the explanation of his erroneous testimony that his "M.S.P." salary was not included in the overhead allocated to the corporations in receivership, and in his testimony as to the meaning of his statements on the Manning trial in Delaware. With these possible exceptions, he appeared through the long weeks on the stand, frank and honest in testimony and thoroughly convinced of the good faith of his every action in the receiverships. Moreover, many of the individual actions attacked by the objectants turned out to be convincing illustrations of Glass' good faith in dealing with the trust. The readjustment of inter-corporate claims after reorganization, in May, 1930, for instance, operated to the disadvantage rather than to the advantage of M.S.P. The appraisals and the eventual realization by M.S.P.'s subsidiaries from the sales in the ancillary jurisdictions are convincing proof of meticulous care that the sellers be treated fairly. So also with the comparative price paid receivership estates and outsiders for similar securities purchased by M.S.P. Some of Glass' transactions may have been harmful to some of the receivership estates. If so, the Court is convinced that they were not the result of active fraud or attempts to despoil the receiverships for his own benefit or that of M.S.P." Although it is of course true that such a finding is not exempt from review by us, "it is not enough that we might give the facts another construction, resolve the ambiguities differently, and find a more sinister cast to actions which the District Court apparently deemed innocent." * We have again and again laid especial weight upon the importance of findings that touch the good faith and honesty of a witness, whom the judge has seen; for, as we have said, on such occasions the printed record does not preserve a part of the

---

* *United States* v. *National Association R. E. B.*, 339 U. S. 485, 495.

BLEED THROUGH POOR COPY

evidence, which on that issue is often crucial. To ascertain another's motives we are of necessity driven to inferences, for they are never manifest to our senses; no one can see, hear or feel what has actuated someone else. Among the sensible facts on which we must rely is the manner in which the witness utters his testimony: *i.e.*, his address and bearing, his frankness, his directness and freedom from evasion, his assurance as to what he has personally observed, and his readiness to admit his uncertainty as to what he has not: all these things are among the most convincing means of deciding whether to believe his testimony. And so, when a judge of tried experience has had the opportunity to observe a person through days of the most searching and provocative cross-examination; and when he has made findings and written an opinion that show the most painstaking and impartial solicitude to reach the truth, his decision about that person's motives is nearly conclusive; and we should disturb it only when the objective circumstances make it clear that the unpreserved evidence could not have properly overbalanced the inherent improbability and inconsistency of his spoken words. We can find nothing in this record that would sustain such a conclusion as to Glass. The "Bondholders' " brief abounds in charges that gravely impugn his honesty, and impute to him a ruthless disregard of his duty to the creditors of "U.O.P.," or of the other subsidiaries. Were they true, nothing could excuse him; but, so far as we have discovered, there are none that furnish any affirmative proof against him. It is quite true that, once one assumes that he was bent upon forcing all to join the reorganization, what he did was consistent with that purpose, but that is altogether irrelevant, if it was equally consistent with innocence, as it was.

It would take too long to go over in detail all that is mustered against him; but one or two illustrations may

deserve notice. The brief repeatedly asserts that Glass had planned to become president of the new company a good while before the sale of the "U.O.P." assets in 1929; and that his letters covertly betray this wish. On the contrary, the letters bear every evidence of an unwillingness to be president, though they quite frankly declare that he would like to be the lawyer for the reorganized corporation. Take for example this passage from a letter written in October, 1927, to one, Gilbert, a banker in Oklahoma: "I have personally reached the definite decision that I do not care to continue with the reorganized company in any executive capacity, as I do not feel that I would want to subordinate my professional practice to the daily necessities of a going business, and I feel that if I were to attempt it, the company's interests would suffer. The only relationship on my part with the company in the future that will be possible, as far as I am concerned, will be a professional relationship, if my legal services should at any time be required." Conceivably such language might have been used to disarm opposition while Glass was in fact intriguing to get the job; but on what imaginable ground can it be taken as affirmative evidence that he was doing so? To take it as written in fulfillment of such a clandestine purpose is completely to pervert its natural meaning.

Again, take the agreement that the "Receivers" got from the reorganization committee in the following terms: "It is the understanding of counsel for the Reorganization Committee that the acts of any persons who are employees of the Receivers and are permitted by them to participate in such action of the Boards" (*i.e.* "resolutions authorizing the filing of answers admitting the allegations of the bills of complaint") "shall not be deemed the action of the Receivers or action taken on their behalf; and that the action of the respective Boards * * * shall in all respects be without prejudice to the right of the Receivers to raise

BLEED THROUGH POOR COPY

any question with respect to the subject matter of said suits or any of them in the event that the Reorganization Plan as now existing or hereafter amended shall fall through." Of this the "Bondholders" say in their brief that it "of course * * * meant that these judgments and decrees, though absolute on their face, were subject to be vacated at the instance of the Receiver if the plan was not carried out. It is difficult to see, therefore, in view of all the circumstances, how this sale was not collusion or 'hocus-pocus.'" As we understand this argument, it means that the "Reorganization Plan" would have "fallen through," if an outsider had appeared at the sale and outbid the reorganization committee; and that in that event the "Receivers" had the option of vacating the decrees on which the sale was made. In the first place the "Plan" would not have "fallen through," if that had happened, for it was a condition precedent of the "Plan" itself that they should be offered to outsiders, and that, if a bidder appeared, who should outbid the reorganization committee, the properties should pass to him. The "Plan" would not in that event have gone into effect, but the properties would have passed beyond the power of the court, exactly as it was intended they should. The "Plan" would not miscarry, if the prescribed alternative to it had been realized. In the second place even if we impose that meaning on the words, "fallen through," the agreement did not give the "Receivers" the power to "vacate" the "judgments and decrees." All it did was to provide that the "Receivers" should be free to take such action as seemed to them to be for the best interest of the defendant corporations, regardless of the fact that the "action of the Boards" in consenting to any "judgments and decrees," might have required the votes of employees of the "Receivers." It was plainly no more than a precaution—probably unnecessary—to retain whatever power they had had to provide for

any occasion that might arise after a breakdown. How it can be thought to have been any evidence of conspiracy to seize the properties we cannot understand.

Finally, although we are prepared to make large allowances for the heat of advocacy in a litigation that has engendered so much feeling, we cannot pass without mention that part of the "Bondholders'" brief that imputes to Judge Smith a partiality in favor of the "Receivers." For example: "The Trial Judge treated the Receivers with the utmost tenderness, resolving every question of fact, every adverse inference in favor of the Receivers and granting them a clean bill of health, whereas the objectants and their counsel were subjected to express and implied unwarranted criticism." It is curious to find this charge supported by the amendment to the 79th Finding of Fact, from which at the "Bondholders'" demand the judge deleted the adjectives "reckless" and "careless" that he had originally used to characterize their conduct, and which, as it now stands, criticizes equally that of both parties. Again: "Yet we are compelled to submit most earnestly that he apparently had a blind spot when it came to judging the Receivers' conduct, particularly Glass'." It is indeed always proper for an appellant to show that the trial judge was guilty of partiality, or of any other judicial impropriety relevant to his decision, and, indeed, nothing can more justly move an appellate court to reverse; but it is a charge that gravely miscarries when it is not made good; and it would be difficult to imagine less support for it than in the case at bar, where the record throughout shows a patience and will to do even-handed justice, that might serve as a model for imitation anywhere.

However, although we put aside, as we do, the charge that Glass was a party to any fraud or conspiracy, we agree with the "Bondholders" that the burden would nevertheless be upon him to prove that they had suffered no

BLEED THROUGH POOR COPY

actionable loss by any of his acts or decisions in which he could have been actuated by a personal interest that conflicted with his duty to them. Moreover, in that event it would not relieve him of the burden even to prove, if he could, that his putative interest did not in fact influence him, for the law will not attempt to weigh how far such an interest may have played a part in the result, once it be shown to have existed. What we said on the first appeal we repeat with equal emphasis. Nevertheless, before the burden of proof shifts, the beneficiary must prove that there was such a conflict; it therefore rested on the "Bondholders" to prove that Glass had some personal interest in putting through the reorganization that conflicted with his duty as receiver. In considering that question we must at the outset distinguish between an occasion where the conflicting interest is personal to the fiduciary, and one where it arises between two or more of his beneficiaries. For example, in the case at bar the "Bondholders" repeatedly complain that Glass failed to pay the interest on the "U.O.P." bonds at times when that company was in adequate funds to do so. This, they argue, was because he preferred the interest of "M.S.O." which at the time he thought had more pressing need for the money. To a similar charge Judge Smith made what we regard as the proper answer; it might be true, he said, that "in some instances such as failure earlier to realize on the collateral behind the Chatham-Phenix note he" (Glass) "was unconsciously influenced by a desire to benefit the group of receiverships as a whole and later M.S.P., rather than to act solely for the benefit of the estate of Western. That was a danger incurred by the Court in order to avoid the expense of some thirty-eight additional receiverships. If it did occur and cause damage to the estate of Western, some means must be found to rectify it." But he did not include among those means a surcharge of Glass on the theory that he was

a fiduciary subject to a conflict of interests. Similarly, assuming for argument that there were moneys of "U.O.P." that Glass might have used to pay the interest on its bonds, his interest, as receiver of "M.S.O.," which owned directly or indirectly substantially all of "U.O.P.'s" shares, even if it conflicted with that of the "U.O.P." bondholders, was a conflict inevitable in the set-up of 38 or 39 receiverships all conducted as one. Glass owed the same duty to "M.S.O." as to "U.O.P."; both duties had been imposed upon him by the court, and he was not only free, but bound—if they conflicted—to decide which need was the more imperative. It must be remembered that the "U.O.P." bondholders had no legal interest in the income as yet; as mortgagor, that company was free to use its income until the mortgagee, the indenture trustee, moved to sequester it for the bonds.

Nor was it necessary for the "Receivers" to procure an order of the court whenever a conflict of interest arose between any of the 38 corporations with custody of whose assets they had been entrusted. The interests of all were so enmeshed that countless transactions were likely to involve "U.O.P." with "M.S.O.," or with one of its subsidiaries, that the court would have been obliged constantly to intervene in the administration of the suits. That was exactly what Judge Knox meant to avoid, because as Judge Smith found: "During the receiverships * * * temporary loans were made by the receivers * * * from one receivership estate to another. This was done without Court order in reliance upon the order of appointment, requiring the properties and business of all the companies to be administered as an entirety." Moreover, even if it had been a fault not to get an order, the "Bondholders" have not shown that Judge Knox would not have granted leave to use the money, so that no loss was shown; and they had the burden

BLEED THROUGH POOR COPY

of proving that they were damaged, so long as the "Receivers" had no personal interest in the decision.

However, there were other occasions when the "Bondholders" assert that Glass had a personal interest that conflicted with his duty, which if they were right, would have shifted the burden of proof. The first of these is as follows. Glass had been a member of the firm that had represented Shivers, the plaintiff in a shareholders' suit against "M.S.O." commenced in 1924. All that was ever done in that suit was to move for a receiver, which was denied; and almost at once Phelan, a creditor of "M.S.O.," filed the suit against "M.S.O.," followed by the others of which the action at bar is one. The services of the firm in this shareholders' suit could hardly have had any but a trifling value; but in any event they stand or fall with the services in the creditors' suits themselves. All these were of the type common thirty years ago before the amendments to the Bankruptcy Act, or the passage of the S.E.C. legislation. They were a variant of the long existent judgment creditors' bill in equity, and were designed to effect an equal distribution of a corporate debtor's property among its creditors. They usually alleged that if this was abandoned to a scramble of attachments and executions, the creditors generally would be losers; and the jurisdiction in equity rested upon this circumstance. Since originally such a bill lay only after judgment and was to reach assets not subject to execution, it was necessary before judgment for the debtor to consent to the appointment of a receiver. In the case at bar after the "Receivers" were appointed, the debtor's creditors in all 38 suits formed committees, and Glass's firm represented them in all, so long as Judge Mayer remained in office. After his death Glass was substituted in his place, and his firm at once ceased to represent any of the committees. The "Bondholders'" argument is that, since the firm's allowance, as

counsel for these committees, had not been fixed before the sale of "U.O.P." assets in December, 1929, and since he therefore retained an interest in what should be allowed, he had a personal interest that was in conflict with his duty as receiver. Moreover, the firm had agreed with the succeeding counsel that its allowance should be a proportion of the allowance made to their successors so that Glass became directly interested, not only in what should be allowed for his firm's services rendered before he became receiver, but for those rendered thereafter; and a successful reorganization would be likely greatly to enhance his allowance. A complete answer to this is that not only Glass, but Jackson, a member of the succeeding firm, swore that this agreement was made in 1930, after the sale of the "U.O.P." assets, and after "M.S.P." had undertaken to pay all expenses of the receivership. We can find no testimony to the contrary and Judge Smith's general acceptance of Glass's credibility serves in place of a finding. It was still true that all through his receivership and up to the sale, Glass's allowance remained undetermined, but we cannot see that that created an interest with which a sale as opposed to a reorganization would conflict. The argument must be that Glass's firm, as attorneys for the creditors' committees, performed services during the first year of the receivership, the allowance for which would in some measure depend upon whether five years later a reorganization went through. That appears to us too remote and speculative a conflict to fall within the doctrine invoked by the "Bondholders." We shall deal more at large with the general question in a moment when we come to Glass's hope to be counsel for "M.S.P."

The second supposed conflict between Glass's duty and his personal interest was this. His firm had retained one, Hamburg, to take charge of extensive tax claims against "M.S.O.," of course including "U.O.P." It was part of the

BLEED THROUGH POOR COPY

agreement that Hamburg should assign a proportion of his allowance to the firm, in place of paying rent for the use of their offices. We cannot see that the amount of Hamburg's allowance would have been larger if "M.S.O." was reorganized, rather than if the properties were sold to an outsider. The allowance was an expense of administration and had to be paid in either event. Had it been liquidated before the sale, Glass would indeed have had an interest in not opposing it, but it was not. Moreover, even then the conflict would have tainted, so to say, only the allowance granted Hamburg.

The third alleged conflict is that Glass had a covert understanding that he was to be president of "M.S.P." when formed; and, in default of that, that he hoped and expected to be its counsel. We have already indicated that Judge Smith's findings as to the future presidency of "M.S.P." are, not only not "clearly erroneous," but that the attack upon them is without any support whatever in the evidence and is indeed positively contradicted by contemporaneous correspondence. It is not necessary to do more in disposing of this charge than to quote the findings themselves. "A month and a half after the organization of the new company, and after ascertaining that the Court had no objection" (to) "Glass' serving as president of the new company, on an understanding with the company that, in any case in which the company's interest conflicted with his position as receiver, he would act as receiver and not for the company, Glass accepted election as president of the new company. He had not actively sought election to the position, having made known his desire to terminate his management responsibilities although he hoped to continue to be associated in a legal capacity with the new corporation. Search on the part of the members of the reorganization committee for an experienced oil man to head up the new company was, however, unsuccessful and

by the offer of a salary of $50,000 a year, with the right to continue his law practice, Glass was induced to continue as the executive head of the reorganized company."

The fourth and last supposed conflict was that Glass hoped and with good reason expected to be chosen counsel for "M.S.P." when it was reorganized; and that he had no such expectation if the Eureka shares were knocked down to an outsider. True, it did not follow that such a putative outsider might not have wanted him as counsel, but that we disregard as too remote. Moreover, we agree that although he had no contract with the reorganization committee, he had good reason for thinking that "M.S.P." when organized would follow the obvious preference of the committee and offer the job to him. Was that such a conflict as invokes the doctrine? It enables the beneficiary to hold the fiduciary liable for any profits he may make, or losses he may cause, in order to deprive him of any inducement that will affect his absolute and disinterested loyalty; and there is no doubt that an expectation or hope of future advantage may do so, even though it is not secured to him as an existing legally protected interest. Therefore, if the doctrine be inexorably applied and without regard to the particular circumstances of the situation, every transaction will be condemned once it be shown that the fiduciary had such a hope or expectation, however unlikely to be realized it may be, and however trifling an inducement it will be, if it is realized. We do not understand that it is to be applied so rigidly, or to so literal an extreme. The Restatement of Trusts* states it in these words: the "trustee violates his duty to the beneficiary not only where he purchases trust property for himself individually, but also where he has a personal interest in the purchase of such a substantial nature that it might affect his judgment in

* § 170, Comment (e).

BLEED THROUGH POOR COPY

making the sale." And this has been incorporated *in ipsissimis verbis* into Scott on Trusts.* That statement we accept, and the question at bar is whether Glass's expectation of being counsel was an interest so "substantial * * * that it might affect" his promoting as much as he should have done, the sale of the Eureka shares in place of including them in the reorganization of "M.S.O." It is true we cannot know that the chance of employment could not have had any influence upon his conduct; and it is of course true that, if the "Bondholders" had shown that in fact it did have any, he would not only have to disgorge any profits he had got, but to prove that what he did was an impeccable discharge of his full duty, or to make good any loss that it caused. But we are not dealing with such an occasion; we have to determine the scope of the implementary rule that dispenses with the need of proving that his personal interest had any part in determining the fiduciary's conduct; indeed, with a rule that altogether forbids any inquiry whether it had any such part. We have found no decisions that have applied this rule inflexibly to every occasion in which the fiduciary has been shown to have had a personal interest that might in fact have conflicted with his loyalty. On the contrary in a number of situations courts have held that the rule does not apply, not only when the putative interest, though in itself strong enough to be an inducement, was too remote, but also when, though not too remote, it was too feeble an inducement to be a determining motive.

In *Bullivant* v. *First National Bank*, 246 Mass. 324, 334, shareholders of a company who had deposited their shares in trust with a bank sought to enjoin it from voting the shares for a proposed reorganization of the company, because the bank, as a creditor, had a conflicting interest that

---

* § 170.10.

disqualified it from voting. The court held otherwise, saying that the "facts reported by the master did not disclose any proposed violation of this rule": *i.e.* that a "trustee cannot become purchaser of property title to which he holds in his capacity as trustee." In *Anderson* v. *Bean,* 272 Mass. 432, 446, the trustee held all but three of the 6000 shares of a corporation—half, as trustee, half, individually. He sold 100 shares of those that he held as trustee: 25 to his son, 25 to each of the sons of a deceased brother, and 25 to the superintendent of the factory. The beneficiaries sought to charge the trustee with the value of the 100 shares above their sale price on the ground that by their sale he had gained a personal advantage: *i.e.* control of the corporation. The court disallowed the surcharge, saying that the "disturbance of the equal balance of holdings of stock by the trust and by the trustee as an individual is not as matter of law, apart from other circumstances, unconscionable advantage or disadvantage." It agreed that a trustee "cannot derive any personal advantage at the expense of the estate, nor put himself in a position antagonistic to the beneficiaries of the trust"; but that that doctrine "simply is not applicable to the facts here disclosed." Yet, surely voting control "might" very easily "affect" a fiduciary's "judgment," if we are dealing in all possibilities, however remote. In *In Re Harton's Estate,* 331 Pa. St. 507, 515, 516, a trustee invested part of the fund in a participation in a mortgage; and at the same time "undertook the task of acting as rental agent for the mortgagor and received from him a commission of five per cent on rentals so collected." As to this the court said: "The compensation received by the trustee as rental agent for the owner was not money which the participating trust interests would otherwise be entitled to. They would have belonged to the owner, or would have been paid out to some other rental agent as fair compensation for services ren-

BLEED THROUGH POOR COPY

dered. It was not shown that the rental commissions were in any sense a profit; on the contrary, they were just charges for services performed by accountant in its required administration of the trust, and their receipt does not offend the admitted rule against a trustee's obtaining a bonus or commission from dealing with specific trust property, as commented upon in American Law Institute, Restatement of Trusts, §§170 and 203, pp. 438 and 549." *Pike* v. *Camden Trust Co.*, 128 N. J. Eq. 414, 422-424, involved substantially the same situation and the decision was the same; indeed, it relied upon the passage from *In Re Harton's Estate* that we have just quoted. In *Dabney* v. *Chase National Bank,* we said:* "It is not every possibility, however remote, of a conflict of interest between a trustee and his beneficiary which will forbid his entering into a transaction with a third person. * * * There must come a point at which he is not bound to take against himself a future chain of events, each link of which carries a substantial coefficient of improbability. * * * The law ought not make trusteeship so hazardous that responsible individuals and corporations will shy away from it. As we said in *York* v. *Guaranty Trust Co.*, 2 Cir., 143 Fed. (2) 503, 514: 'Of course, the courts should not impose impractical obligations on a trustee. Merely vague or remote possible selfish advantages to a trustee are not sufficient to prove such an adverse interest as to bring his conduct into question.'"

The trustee's advantage in *Dabney* v. *Chase National Bank, supra,** was security for a loan, and the increase in its value was indeed very "substantial"; but our decision rested on the unlikelihood that the increase would ever be realized. In the two Massachusetts cases the advantage was immediate and certain, but the court thought

---

* 196 Fed. (2) 668, 675.

it too insignificant in value to count; and in the other two decisions the advantage was employment by the purchaser, just as it was here; and, indeed, the trustee had actually been engaged and thus had a legal right to the job. Moreover, as in the case at bar, the advantage was obtainable only by means of a *quid pro quo*—services to be rendered—which of course diminished its inducement. Finally, we should remember that, although Glass was indeed reasonably sure to be retained, nevertheless he had no contract and his employment depended upon what the administration of "M.S.P." might decide. It appears to us most undesirable upon all possible occasions to forbid a purchaser of property from a fiduciary to continue him in its management, upon the assumption that the prospect of getting the job may taint the purity of his decision to sell. Again and again it must be in the interest of the purchaser to keep him; and that possibility may contribute to give the property a greater value than it otherwise would have. Taking the situation in the case at bar as a whole, we do not believe that the prospect of a retainer by "M.S.P." was a "personal interest * * * of such a substantial nature" as was likely enough to cause Glass to fail in his duty to promote the sale of the Eureka shares, and to throw the burden of proof upon him; and we conclude, not only that the "Receivers" were not parties to any fraud or conspiracy against the "Bondholders," as Judge Smith found; but also that the "Bondholders" had the burden of proving that they had lost through some dereliction of Glass in his duty to them as receiver of "U.O.P." It was of course open to them to prove that the "Receivers" did default in the discharge of their duty, and what they did lose; but in a situation so extravagantly complicated and so impervious to analysis as the welter of legal rights and obligations left by Haskell and his fellows, the party that has the burden of proof is nearly sure to lose.

BLEED THROUGH POOR COPY

The "Bondholders" do allege that they showed affirmatively that the "Receivers" did fail to discharge their full duty, and that they have shown what was their loss and at least Glass's profit. This they claim to have proved as to Glass in two respects: (1) that he was party to fixing the minimum prices of the "U.O.P." assets too low; and (2) that he not only failed to give adequate publicity to the sale, but that he actually "chilled" the bids. We repeat what we said upon the first appeal, that a receiver "is 'bound to act fairly and openly with respect to every aspect of the proceedings before the court. * * * The court, as well as all the interested parties,' have 'the right to expect that all its officers,' including the receiver, will not 'fail to reveal any pertinent information or use their official position for their own profit or to further the interests of themselves or any associates.'* A receiver has the 'affirmative duty to endeavor to realize the largest possible amount' for the assets of the estate.** If he has vital information which, if disclosed, might bring a better price for the property * * * he must fully disclose it 'prior to the sale when the prospects (are) greater for successful bargaining.'" † It is with these principles in mind that we will consider what the record discloses as to both the faults charged against Glass. First, as to the minimum prices that the reorganization committee—with the consent of Glass—fixed for the sale of the "U.O.P." assets. These consisted (1) of all the shares in the Eureka company, which held 82.44% of the shares of the Turman Company, which in turn had three extremely profitable leases in the Oklahoma oil fields; (2) of a guaranty by the Imperial Oil Corpora-

---

* *Crites, Inc.* v. *Prudential Co.*, 322 U. S. 408; *Woods* v. *City Bank Co.*, 312 U. S. 262, 263.

** *Jackson* v. *Smith*, 254 U. S. 586, 588.

† *Phelan* v. *Middle States Oil Corporation*, 154 Fed. (2) 978, 991.

tion, and (3) of the intercorporate claims of "U.O.P." against "M.S.O." and a number of its subsidiaries, which, though not pledged to the bondholders, as were the Eureka shares, were nevertheless security for any deficiency under the mortgage because the bondholders were substantially the only creditors of "U.O.P." The price fixed by the committee for the Eureka shares was $1,450,000, and Judge Smith found that it was "fair." The "Bondholders" challenge this finding and the question is whether his finding is "clearly erroneous." In appraising the shares the judge adopted four possible approaches; of which, however, we need concern ourselves with only two, for he found that "of the various balance sheets in evidence, those entitled to most weight in determining value are those based on capitalized earnings and contemporaneous market values of stock." There was no evidence of quotations of actual sales of Turman shares during 1929; only of the bid and asked quotations, and it is quite true that these are not very reliable sources for "contemporaneous market values of stock." Indeed, in New York apparently they are treated as wholly incompetent.* However, under Federal Rule 43 (a) evidence, incompetent under the law of the state where the trial is had, may yet be received in a federal court; and we do not see why actual asked prices in accepted publications should be utterly incompetent as evidence at least of maximum values, in absence of evidence impeaching their good faith. True, bid and asked prices give us nothing but the extremes between which sales, if any, will take place, but it seems to us that the asked prices may be taken as some evidence that the value was no higher. The asked price for Turman shares, from April 10 to October 10, 1929, was between $4 and $8; and between

* *Wildes* v. *Robinson*, 50 App. Div. 192; *Beardsley* v. *Nieblo Manufacturing Co.*, 231 App. Div. 152.

BLEED THROUGH POOR COPY

October 10, 1929 and April 10, 1930, it was between $4 and $6. No doubt any attempted appraisal can be only approximate; but we cannot say that $4 was a "clearly erroneous" approximation, in face of the fact that throughout this year nobody appears to have been willing to offer more than $5 for the shares.

Be that as it may, in several decisions* the Supreme Court has treated as a particularly reliable method of appraising the value of corporate shares (we assume this to presuppose the absence of actual sales upon an open market) the capitalization of the "reasonably to be anticipated earnings" of the corporation; and we have read these cases as laying it down "that the best test of the value of a going commercial enterprise is its earning capacity."** What is the proper coefficient to apply to the earnings the Court naturally has never made any attempt to declare; obviously it must vary with the nature of the business, and in the case of a wasting asset, like an oilwell, it will be much higher than in an ordinary industry, because the earnings then include part of the capital. The earnings of the Turman company for the five years preceding 1930 had varied greatly owing to the fact that in 1927 some new wells went into large production. The net income for the three years 1927, 1928 and 1929 (disregarding for the moment any "non-recurrent" disbursements) was about $1,057,000, or an average of $352,000. On the other hand the years 1925 and 1926 had shown a net loss of about $64,000, so that if the whole five years are considered together, the average becomes what Judge Smith found it to be: $198,519.57. Moreover, the average income for the five years from 1929

---

* *Galveston, H. & S. A. R. Co.* v. *Texas*, 210 U. S. 217, 226; *Consolidated Rock Products Co.* v. *Du Bois*, 312 U. S. 510, 525, 526; *Group of Institutional Investors* v. *Chicago, M., St. P. & P. Ry.*, 318 U. S. 523, 540.

** *Dudley* v. *Mealey*, 147 Fed. (2) 268, 270.

to 1934 inclusive was $81,403.38. However, since the five years that followed 1929 were those of the Great Depression, the "Bondholders" with some warrant protest against their inclusion, for, although all values began to melt in October of 1929, no one in December "reasonably anticipated" the extent of the collapse that followed. On the other hand, it would be unfair to take the three productive years 1927-1929 inclusive as a proper measure of the future, for no one could know how long the new wells would last; and indeed, the income for the year 1928 was already only a little more than 75% of that for 1927, and that for 1929 was still less. The year 1925 resulted in a loss of over $111,000; and, if it be thought unfair to include it, certainly it would be permissible to take the four years 1926-1929 inclusive: which gives an average of about $276,000. At a coefficient of 10 this would of course make the value of the Turman shares $2,760,000 of which 82.44% owned by Eureka would be $2,275,000, of which $1,450,000 is less than 64%. On the other hand the average coefficient of appraisal in the case of nine oil corporations comparable with Turman was 19.31, and that, even though it were applied to the average earnings for 1926-1929 inclusive, gives a value of less than $1,430,000, of which 82.44% is only a little more than $1,100,000. Indeed, if the lowest coefficient of six of the nine companies—15—be taken, the value of the Eureka proportion is only about $1,500,000. Plainly therefore $1,450,000 was not a "clearly erroneous" figure to set as a "fair" price under this hypothesis.

The "Bondholders" complain of the omission from the computation of the average annual income of the Turman company of what they call the "non-recurrent" items appearing upon one of their exhibits—No. 170. Some of the items deducted appear to be such that they would have had, at least in part, some equivalents if the Eureka company had not been in receivership; from the face of the

BLEED THROUGH POOR COPY

exhibit it is impossible to say that under another name they might not have been a usual corporate expense. However, suppose we accept them all as they stand, as "non-recurrent," and take an average of income for five years, and, for a coefficient, the average, 19.31. At the average for five years—$374,000—this would make the Turman shares worth substantially $1,800,000, of which 82.44% is $1,484,000. And even though we count only the four years, 1926-1929 inclusive, so that the average income was $414,-500, the value of the Turman shares was less than $2,150,000, of which 82.44% is $1,775,000, of which in turn $1,450,000 is more than 80%. Certainly, 20% of the price that a seller would take at an unforced sale is not an unreasonable discount for a price at a forced sale at auction. Thus, even though we take the "non-recurrent" items at their face, the minimum price for the shares was "fair"; certainly it would be beyond any possible propriety to hold that a finding that it was "fair" was "clearly erroneous." On the whole our guess is that it bordered on the high side.

The only other assets of "U.O.P." were the guaranty of the Imperial Oil Company and its claims against "M.S.O." and the other corporations in the Haskell System. We shall include these together in our discussion, for the same considerations govern the disposition of each. Two orders were entered, one, on December 14, 1929, and the other, in May, 1930, professing to liquidate the intercorporate claims of the various enmeshed companies. The "Bondholders" protest that these orders are not conclusive; and, although we do not find it necessary to hold whether they were, we will assume for argument that they were not. They were nevertheless bona fide efforts to learn what were the mutual credits and debits; and we accept them as some evidence of what the claims were; certainly they are the best available. We need consider only the three largest claims of "U.O.P.": that against "M.S.O." for nearly $1,400,000; that

against Reliable Securities Corporation for about $2,000,000; and that against Imperial Oil Corporation for about $2,250,000—a total of over $5,500,000. The first question is whether it was proper to sell these claims without some authoritative settlement of their validity and amount. In the ordinary case it might indeed be true that it was not proper, for obviously, until then bidders could not know what they would get if their bids were accepted. However, this was as far as possible from being the ordinary case. The receiverships had been going on for five years, during which the "Receivers" had been making continuous efforts to find out what were the mutual rights and liabilities of the maze of corporate entities. Judge Smith found that "the books of the companies were either non-existent or inaccurate. Advances had been made between the companies, proceeds from the sale of stock recorded as income from oil sales, and other irregularities existed." As early as November, 1924, an accounting firm employed by an engineering firm, which in turn the "Receivers" retained, had reported that the part of their work "by far the most difficult of accomplishment" was to "develop a history of transactions affecting capital stock and bond issues, the acquisition of properties and securities, and establishing the considerations paid, as well as real intrinsic values thereof; ascertain dividends declared and paid, determine present ownership of leaseholds and if possible ascertain the earnings and expenses since incorporation in 1917." To this the accountants prophetically added that "the possibility looms up that all the real facts will never be entirely disclosed." In June of 1925 the "Receivers" reported to Judge Knox that the books, records and accounts of the Middle States Oil Corporation and its subsidiaries prior to the 1st of January, 1924, were so incomplete, complicated and confused that it was impossible readily to ascertain approximately the financial condition of the com-

BLEED THROUGH POOR COPY

panies or their true financial relation to one another." It is quite true that in May, 1928, nearly three years later, they reported that "inventories of all physical equipment * * * have been completed" and that "valuation engineers are now at work completing their appraisals of all of the leaseholds" which "will be used as the basis for proper book entries as of January 1, 1928." It was their purpose "to thereafter present recommendations to the Court for the disposition, without litigation, of these intercorporate accounts upon notice to all interested parties." They felt it their duty, they said, to have the companies come out "with their affairs in order. To bring such a condition about, from the lack of record and the chaos as to existing record which the receivers found * * * has been a mammoth task." "Fortunately the end is in sight. The complications which remain are few in number. The facts with respect to them have been clarified." Nevertheless, they added that the "solution depends in large part upon the common sense attitude of the parties involved, in working out adjustments as between themselves. If they fail to apply common sense, then they will have themselves only to thank for any delay in the resumption of the business affairs of these companies." It turned out that the hopes of the "Receivers" that the parties would adopt "common sense attitudes" were not realized, and Judge Knox had already become very restive at the continued delay, for, beginning in March, 1928, he several times expressed his "grave concern" at the accumulating cost; and on March 3, 1929, he summoned the "Receivers" and the committee to appear before him on the 9th and discuss "various features of the case." There followed a number of hearings at all of which Judge Knox pressed both the "Receivers" and the committee to prepare a plan of reorganization that might put an end to the extreme waste that kept on. Judge Smith found that the "Court pressed for action looking toward reor-

ganization and termination of the receiverships, insisting in early 1929 that positive action be taken." He also found that "delay in reorganization would have run the costs up so that the chance of any organization surviving would have disappeared."

It is against this background that the action of the committee with Glass's concurrence is to be judged. We do not mean to intimate that Judge Knox was wrong in insisting that the Gordian knot must be cut at any cost; but we do mean that, right or wrong, as to Glass at any rate his decision was imperative; for it would be patently absurd to hold a receiver liable for complying with an order that was within the jurisdiction of the court that appointed him. Therefore, whatever were the consequences of selling the claims before they were liquidated, and however necessary liquidation ordinarily may be, Glass's liability is to be judged by whether he did the best he could within the limited time granted him. Nor can we find any evidence that he concealed from Judge Knox anything that bore upon the situation. His reports, after he became receiver, were very full, and he was in constant communication with the judge. The chief basis of the charge of concealment is that he did not tell Judge Knox of his conflicting personal interests, and as we have seen, there were none such. Incidentally, Glass gave evidence of a proper sensitiveness upon the score of divided loyalty after he accepted the presidency of "M.S.P.," though still a receiver. True, there was an inevitable conflict of interest between the corporations whose claims were being appraised, for any reduction in the credit of one was a release of debit to another; but, just as in the case of failing to pay interest upon the "U.O.P." bonds, these were conflicts that the very nature of his duties required him to decide; and they can be charged to him as a fault only by a misconception of the meaning of the doctrine invoked.

BLEED THROUGH POOR COPY

We must therefore accept it as an inescapable condition that some value had to be set upon the claims of "U.O.P." against "M.S.O." and its subsidiaries within a period that did not allow any authoritative liquidation. We cannot see what more either the committee or Glass could do than to make the best approximation that was available; all that was open to them was a "solution" that depended "in large part upon the common sense attitude of the parties involved in working out adjustment as between themselves." In short, they were bound to do the best they could within the time they had even though the result were no better than a guess. There is not the slightest evidence that this is not exactly what they did; although the claims due to "U.O.P." on their face were for the very large amounts we have mentioned, they appraised them at only $300,015, of which they took $200,010 as a fair minimum price. This appraisal depended upon the labyrinth of cross claims between the corporations making up the "M.S.O." system; and we do not know how they were reached, nor is it necessary that we should; they stand unless they are shown to have been incorrect and they have not been. Moreover, even were we to match our judgment against that of Judge Smith, it would be the height of presumption for us to say that his approval was "clearly erroneous."

In one respect it is true that his finding does open a question for our review. A price was apparently first fixed at what was called the value of an asset for "reorganization purposes," meaning its value to a going concern, and the minimum price was fixed at two thirds of that amount. In the case of the Eureka shares the question does not arise whether this was too large a discount because, as we have shown, there was ample evidence justifying at worst an appraisal of which the minimum price was 80%—a discount too obviously proper to need any defence. In the case of the guaranty and the intercorporate claims, al-

though there is indeed no such objective test, the nature of the property was such as to make a large discount inevitable. In order to judge the propriety of the appraisal for "reorganization purposes," let us first assume that "U.O.P." wished to dispose of all the intercorporate claims, being free to keep them, if it did not get a satisfactory price; but, nevertheless, desiring to do so without authoritative liquidation. Such was the occasion on which $300,015 was set as a fair price for the claims, which, as we have said, it was not "clearly erroneous" for Judge Smith to accept as "fair." Let us then contrast this with the "fair" price at a forced sale at auction. "In business life forced sales for cash are such a last resort for obtaining money that a sale 'under the hammer' is synonymous with a sale at a sacrifice, and prices obtained at such sales have usually been rejected by courts when tendered as evidence of value." * How then can we say what was a "fair" price when the seller was forced to sell at auction and without any opportunity to bargain? The truth is that any decision inevitably is a speculation, where no more may be demanded than an honest effort to decide questions of validity that have no available answer, and to measure values that are not measurable. That does not indeed mean that a figure could not have been put that was plainly wrong; but any guess that we might substitute would have as little likelihood of being right as the honest guess of those who were very much better informed. The discount of one third, used as to assets of this kind, was within permissible latitudes.

Therefore we conclude that both as to the Eureka shares and as to the guaranty and intercorporate claims Judge Smith's findings that the minimum prices set were "fair" should not be reversed; and there remains only the ques-

---

* *Geddes* v. *Anaconda Copper Mining Co.*, 254 U. S. 590, 602.

BLEED THROUGH POOR COPY

tion whether Glass was delinquent in his duties, as receiver, upon the sale. As we have already said, we can find nothing to warrant the charge that he concealed from Judge Knox any information that he had about the affairs of the company; so that this phase of the dispute depends upon (1) whether the sales of the U.O.P. assets were conducted in accordance with the decrees; and (2) whether the "Receivers" failed to discharge any additional duties to secure the attendance of bidders impliedly imposed on them as receivers. The Eureka shares were sold apart from the "unpledged" assets under the decree of November 15, 1929, entered in a suit brought by the Chatham-Phenix Bank, as mortgagee, to foreclose the mortgage upon them and to enforce the guaranty of the Imperial Oil Company. The "unpledged" assets—*i.e.* the intercorporate accounts—were sold under the decree of November 22, 1929, in one of the creditors' suits brought by Phelan. The foreclosure decree directed the special master to publish a notice of the sale in certain specific newspapers, but the notice itself gave no information about the shares. The decree in the Phelan suit directed the sale of all the "unpledged" assets of U.O.P. as one out of four separate "parcels," and later a sale of this "parcel" together with the three others; the master was to accept the aggregate bid, or the sum of the four bids, whichever was higher. Article Sixth of this decree required the special master to "file with the Clerk of the Court a statement showing and describing as definitely as practicable and made up to the latest day reasonably practicable, but in general terms," the following information: (1) all the assets of the "Holding Companies": *i.e.* "M.S.O.," "U.O.P.," Imperial Oil Corporation and Oil Lease Development Company; (2) all liens and charges by pledge or deposit created by these four companies; (3) all tax claims against them, state or federal; (4) all unpaid liabilities including any executory contracts assumed, or

executed, by the "Receivers"; and (5) all executory contracts made by the companies themselves and still outstanding. The receivers filed such a "statement" in four parts: one for "M.S.O.," one for Imperial Oil Company; one for "U.O.P."; and one for Oil Lease Development Company. That for "U.O.P." stated the cash on hand and the Eureka shares, both as being held as security for the bonds; next it stated certain claims, "amounts undetermined," against the Haskell interests; next, it mentioned "miscellaneous accounts receivable securities and assets believed to be worthless and uncollectible"; next, it mentioned "claims against various subsidiary and affiliated companies for post receivership advances"; next, the three "intercompany claims against subsidiary and affiliated companies" aggregating about $4,500,000; next it set forth the mortgage securing the bonds; next, an "undetermined tax liability, if any"; and finally, it concluded by mentioning all the open allowances "to be fixed by order of the Court," ("undetermined tax liability if any"—a repeat—); "current office salaries and expenses," "claims by various subsidiary affiliated companies for post receivership advances"; no executory contracts of any kind. All the four statements contained the following addendum: "Further information with respect to the foregoing may be obtained upon request at the offices of the Receivers, Room 1401, 170 Broadway, New York, N. Y." In their offices the receivers did have complete records of all the accounts and the results of their work for the five years that they had been in office; and, so far as appears, these would have been accessible to anyone who showed a genuine interest in bidding at the sale.

Judge Smith found that this statement "was wholly inadequate to inform bidders as to the assets to be sold, the receivers' liabilities to be assumed by the bidders, and the status of the government tax claims and the receivers'

BLEED THROUGH POOR COPY

claims for tax refunds." On the other hand, he also found that the "plan of reorganization available since June 1929, had made it plain that all or almost all the tax claims were expected to be defeated and refunds of substantial amounts obtained." True, the statement itself was positively "misleading in that it listed large government tax claims without reference to the favorable progress of the tax litigation"; but it was "unlikely that any prospective bidder would stop at the perusal of the statement without further inquiry of the receivers." In general the "complexities of the inter-corporate relationships, and of bringing down to date the valuations of physical assets and adjusting them to their book listing for the intervening periods were so great that no prospective bidder could have obtained sufficient information to judge independently without assistance from someone in the receivers' organization the value of the assets sold within the period from the filing of the statement to the sales." It would have been wholly impossible within the time allowed to make anything approaching an adequate disclosure of the whole web of claims and cross-claims that a group of utterly unscrupulous stock jobbers had woven before 1924, and that had been continued as a single business by order of the court. Moreover, even if it had been possible, no reasonable bidder would have relied upon it without verification from the documents in the receivers' offices. All that Article Sixth required was that the statements should declare enough to advise all who might be interested as to what was the general character of the property, claims and liabilities that were to be disposed of, in enough detail to send them to the original sources, if they had any serious purpose to buy. Indeed, the article itself required no more than a statement "in general terms." Not only was it impossible to prepare more, but more would have been useless, if it had been prepared. The complaint that all the papers

were not filed in the clerk's office is too trivial to justify an answer. It may be true, as Judge Smith said, that as to the tax liability the statement was, not only inadequate but actually misleading, for taken by itself as it read, it gave no intimation, not only that any liability was unlikely, but that there would probably be a large refund. It does not appear how much of the whole tax controversy affected the interest of "U.O.P.," with which we are alone concerned here; but we will not rest upon that, because we agree with the disposition made of it by Judge Smith: "it is inconceivable * * * that anyone seriously interested in bidding would not have made further inquiry of the receivers."

Since the foreclosure decree required no more than the notice in fact published, the sales were in conformity with its directions, and the question as to the sale of Eureka shares is whether the "Receivers" should either have seen to it that the decree contained more specific publicity, or should, independently of the decree, have done more to procure the attendance of bidders, both as to the shares and the "unpledged" assets. We understand Judge Smith to mean that they did fail to perform their duty, when he said that "no intensive effort was made by the receivers to find outside bidders." This understanding of his meaning is confirmed by the following additional passage: "unless therefore the receivers are to be required to make good an amount in excess of what could have been obtained on foreclosure and receivership sales had they completely fulfilled their duty of disclosure, and active seeking of prospective bidders, there is here no amount to be surcharged for their failure to fulfill that duty." We agree that a receiver is ordinarily under such a duty, but it is one to be measured by the particular occasion; and the scope of any duty is a question of law, not of fact, which we are free to determine as *res nova*. Coming then to

BLEED THROUGH POOR COPY

the measure of the duty to seek out bidders, we note that on September 25, 1928, June 1, 1929, and November 13, 1929, Glass did establish contact with corporations, American or Canadian, which might have been interested in merging with "M.S.O."; and it does not appear that there were any other opportunities for disposal of the assets in whole or in part. The "Bondholders" reason as though the sale had been of a piece of real property, the contents of a house, a retail business, or a completely integrated mercantile or industrial plant. That would be a completely delusive analogy; no casual bidder was conceivable for such property, either of the "Second Parcel"—the "U.O.P." assets alone—or all four "Parcels" together. The only possible bidder for all four "Parcels" would have been some group or combination, already familiar with the oil business in Oklahoma; and it is extremely unlikely that such a group would not have known that for over five years "M.S.O." had been in receivership. Moreover, they would have expected that the receivership would end in some sort of reorganization as a condition of which the assets would almost surely be offered for open sale at auction. It appears to us unreasonable to suppose that any such group would have needed notice of such a sale, involving as it did taking over the whole vast snarl of interrelated corporate transactions during seven years and more of stock juggling. So far as anyone could reasonably anticipate, there would be no market for such an aggregation of rights and liabilities; but, if there was any, the bidders did not need to be alerted. There was even less reason to suspect the existence of any bidders for the "U.O.P." "unpledged" assets sold under the decree in the creditors' suit, for the major part of these was the intercorporate accounts, whose purchaser would have merely bought into an incredibly complicated nest of law suits. Therefore, except as to the Eureka shares sold in fore-

closure it seems to us that the "Receivers" cannot be said to have failed in their duty. As to this property the answer is certainly not plain. True, they were not the kind of property that would be picked up by a random purchaser looking for bargains. Nothing is more uncertain than the life of an oil well; and those who buy them would presumably be already familiar with the business and likely to be aware of new developments. The Seminole fields on which the value of the Turman, and of the Eureka, shares depended had been in rich production for three years, and it seems to us unlikely that any persons who would have been interested in acquiring them would not have learned who controlled them, and that they were to be sold.

If we thought it necessary to decide the question, we might, however, agree with what we understand to have been Judge Smith's conclusion, although it is not a finding of fact, that the "Receivers" did not do their full duty as to the Eureka shares. On the other hand, since the "Bondholders" had the burden of proof to show that this default, if it was a default, resulted in loss to them, and since they have not shown that there were any bidders for the shares, it is not necessary to decide whether there was a default. As Judge Smith said, there was "no evidence, except the receiver's own testimony, as to whether such outside bidders, if found and fully informed, would have made bids in excess of the reorganization committees' bids"; and he accepted Glass's testimony that the value "placed on the mongrel assets" (by which we understand the "unpledged" assets), "for reorganization purposes, was considerably higher than any outside interests could safely or would, with any degree of probability, have bid." Again in the same vein, he said: "Unless, therefore, the receivers are to be required to make good an amount in excess of what could have been obtained on foreclosure and receiver-

BLEED THROUGH POOR COPY

ship sales had they completely fulfilled their duties of disclosure, and active seeking of prospective bidders, there is here no amount to be surcharged for their failure to fulfill that duty." It is true that the "Bondholders" deny that the burden rested upon them to show that some loss resulted from the "Receivers'" fault; they maintain that, as soon as a beneficiary proves that his fiduciary has failed in the discharge of any of his duties, he must clear himself by proving that it caused no loss. However they refer us to no decisions so holding; and of course the ordinary rule as to tortfeasors is the opposite. Moreover, the practice in equity was always to require the beneficiary to prove any "surcharges," which he wished to impose upon a fiduciary; and so far as we have found, no distinction has ever been made between proof of the default and proof that some loss arose from it.* We are to distinguish the well settled doctrine that, when the sufferer from a tort proves that it has caused him some loss, he is not bound to prove its precise amount.** If the "Bondholders" had proved that, if the "Receivers" had searched for bidders further than they did, they would have secured one who would have outbid the reorganization committee, we will assume that that would have been enough; the "Bondholders" would not have been bound to prove by how much such a bid would not have paid the bonds; but they proved the existence of no such bidder. As *res integra,* we can see no reason to extend the implementary rule to occasions, where

---

* *Berner* v. *Equitable Office Building Corp.*, 175 Fed. (2) 218, 220 (C. A. 2); *Palma* v. *Fox*, 182 Fed. (2) 895, 900 (C. A. 2); *Pappathanos* v. *Oakley*, 263 Mass. 401; *Campbell* v. *Campbell*, 8 Fed. Rep. 460; *McManus* v. *Sawyer*, 231 Fed. Rep. 231 (S. D. N. Y.); Daniels Chancery Pleading & Practice, p. #1225; Bates Federal Equity Pleading, Vol. II, § 763.

** *Eastman Kodak Co.* v. *Southern Photo Co.*, 273 U. S. 359; *Story Parchment Paper Co.*, 282 U. S. 555; *Bigelow* v. *RKO Radio Pictures*, 327 U. S. 251.

although the fiduciary has been shown to be in default, the beneficiary has failed to show that it has caused him any loss. It is one thing to do that when the default involves disloyalty to the beneficiary, for that is a violation of the trust that lies at the very root of the relation, a relation that by its nature gives the fiduciary power to act for the beneficiary without his concurrence. But although the fiduciary engages to act in the sole interest of the beneficiary, he does not insure that he will always keep within the limits of his duties. He may misunderstand them; he may be forgetful; he may even be negligent; but he has not been truant to the good faith that he promised to devote to his undertaking. We see no reason why a lapse that does not involve such a breach should throw upon him the duty of disproving a loss that may not have happened at all, and bestow on the beneficiary a windfall to which he may not be entitled if the whole facts could be proved. In such a posture of the proof we can see no reason for not following the usual procedure.

There remains the question whether Glass is liable under the Boyd Rule.* The argument is that the reorganization was illegal because the new securities to be issued against the new assets of "M.S.P." were not equal in tenor and priority to the bonds of "U.O.P." that the "Bondholders" were to surrender in exchange. The Plan proposed an exchange of the "U.O.P." bonds (secured as they were, principal and interest, by the Eureka shares) for "M.S.P." bonds for whose principal and interest all the property of "M.S.P." was liable. Since that property included all the property of "U.O.P.," and also all that of the three other "Parcels," and since no added secured bonds were to be issued by "M.S.P.," there could have been no complaint if the new bonds had been the same in tenor

---

* *Northern Pacific Ry.* v. *Boyd*, 228 U. S. 482.

BLEED THROUGH POOR COPY

and priority as the old. This was however not true: the maturity of the new bonds was accelerated, the future interest was reduced from eight to six and one half per cent, and the accrued interest, amounting to nearly a million dollars, was refunded into a preferred stock—"Class A"—an issue shared with two creditors of "M.S.O.": *i.e.* the "Series Notes" and the "Gulf Coast Claim." In deciding how far this violated the rule, we must of course consider its authoritative statement. At the outset the Court introduced a caveat in these words: "This conclusion does not, as claimed, require the impossible and make it necessary to pay an unsecured creditor in cash as a condition of stockholders retaining an interest in the reorganized company. His interest can be preserved by the issuance on equitable terms, of income bonds or preferred stock";* and in *Kansas City Terminal Ry. Co.* v. *Central Union Trust Co.,* 271 U. S. 445, 456, the Court rephrased this as follows: "whenever assessments are demanded, they must be adjusted with the purpose of according to the creditor his full right of priority against the corporate assets, so far as possible in the existing circumstances." Upon this variant in *Case* v. *Los Angeles Lumber Products Co.,* 308 U. S. 106, 122, the Court appended the following gloss: "where the debtor is insolvent, the stockholder's participation must be based on a contribution in money or in money's worth, reasonably equivalent in view of all the circumstances to the participation of the stockholder"; the final statement of the doctrine is in *Group of Institutional Investors* v. *Chicago, Milwaukee, St. P. & P. R. Co.,* 318 U. S. 523, 565, and reads thus: "It is sufficient that each security holder in the order of his priority receives from that which is available for the satisfaction of his claim the equitable equivalent of the rights

* *Northern Pacific Ry.* v. *Boyd,* 228 U. S. 482, 508.

surrendered. That requires a comparison of the new securities allotted to him with the old securities which he exchanges to determine whether the new are the equitable equivalent of the old. But that determination cannot be made by the use of any mathematical formula." This was reaffirmed in *Otis & Co.* v. *Securities & Exchange Commission,* 323 U. S. 624, 639, 640.

Applied to the case at bar, the relevant inquiry is therefore whether the addition to the property of "U.O.P." of the assets of the three other "Parcels" made the "M.S.P." bonds when issued "an equitable equivalent" of the old bonds. In other words whether the added security so given to the principal of the old bonds was a fair substitute for reducing the future interest, accelerating the due date and refunding the past interest into A shares. Judge Smith found that it was, for he said that the "bondholders received * * * the substantial equivalent of the debt owing to them, both principal and interest," and if this is a finding of fact, certainly it would not be "clearly erroneous." Assuming for argument that it is not such a finding, we must weigh the value of the old securities against that of the new, which it is impossible to do without a better appraisal than is possible of the assets contributed by the other "Parcels": *i.e.* without a liquidation of the intercorporate claims. Thus, as to this question also the answer turns upon who had the burden of proof to show that the conveyance was fraudulent; and there is no reason to impose it upon Glass. To the argument that he was responsible for putting through the reorganization before these facts could be ascertained, we answer, as we did before, that the fault, if it was a fault, was not his, for his orders were peremptory. Considering the means of appraisal accessible to the committee within the time allowed them, there was adequate evidence to support Judge Smith's conclusion, for the exchanges provided in

BLEED THROUGH POOR COPY

the Plan were the result of an honest attempt to take into account the numerous factors that controlled values and, so far as appears, the values assumed were as near the truth as was possible in the circumstances.

It is true, as Judge Smith observed in his opinion, that the Plan was apparently unfair to the creditors of "M.S.O." other than the "Series Notes" and the "Gulf Coast claim," in that they received only shares of B stock in "M.S.P.," part of which was distributed also to the shareholders of "M.S.O." However, he was plainly right in refusing to allow the "Bondholders" vicariously to assert the wrongs of the other creditors. We do not forget that on the first appeal* we said that "the surcharging is not limited to an amount measured by the interest of the particular person thus objecting to the receiver's accounting, since the surcharge is for the benefit of all similarly situated persons. For the court, in administering the estate in its custody for all the beneficiaries, must see to it that none of them suffers because of the misconduct of its receiver, and the discharge of that obligation should not depend upon their appearance in court to voice their objections to that misconduct. Cf. *Moon* v. *Winemann*, 57 Minn. 415, 59 N. W. 494, 495. Thus, if the judge learned of the misconduct from a wholly neutral source (cf. *Investment Registry* v. *Chicago & N. E. Ry. Co., supra*, 212 F. at page 608), he should surcharge the receiver and distribute among all interested the money owing to the estate by the receiver because of that misconduct." This was a note in support of the conclusion that the "Bondholders" should not be barred because of Cohen's possible laches; it did not suggest that Glass could be held liable in this suit to creditors of "M.S.O.," or of any other corporation. The question is

---

* *Phelan* v. *Middle States Oil Corporation*, 154 Fed. (2) 978, 992, note 13.

not whether the conveyance, *i.e.* the reorganization, should be set aside (nobody asks that); it is whether Glass should be held liable because it is not set aside. His liability in the case at bar is as receiver of "U.O.P.," and it is irrelevant that he was also receiver of other corporations in other suits. Any recovery in this suit would of course include all the bondholders of "U.O.P"; but, even though we assume, *arguendo,* that unsecured creditors of "U.O.P." would also be included, that would not serve the creditors of other corporations. Judge Smith's ruling is in entire consonance with the note we have just quoted and we accept it.

The "Bondholders" further object that the option given them to exchange their bonds for the new ones was foreclosed on May 14, 1930. The original date had been five times extended, covering an aggregate extension of four and a half months. During that period, so far as appears, no bondholder asked for any extension, or suggested that he did not have the information necessary to make a choice; nevertheless, the complaint is that the option should have been held open until the dividend in distribution was determined. We answer that, as one extension after another was granted, it should have been evident that there was likely to be a limit, and that such bondholders, if there were any, as were delaying their choice until the distribution dividend was fixed, should have communicated with the committee or the "Receivers," and are in no position to complain that their silence was taken as assent. But we go further. Judge Knox had decided that the receivership, already six years old, must be ended; and if "M.S.P." was to have a start unhampered by the past, it was essential that it should know how many of the old bonds would be refunded and how many it must pay off in cash. That could not be known until the options had expired; and not till then could Judge Knox's decision be put into effect.

BLEED THROUGH POOR COPY

Finally, we should not reverse the judgment on this record, even if the "Bondholders" had proved that the transfer violated the Boyd Rule, and that Glass had made himself a party to the conveyance by his share in preparing it and in recommending its adoption to the chairman of the reorganization committee. That a third party may make himself liable to the creditors of the grantor of a fraudulent conveyance is true;* and apparently the original distinction—which we followed in *Duell* v. *Brewer*, 92 Fed. (2) 59—that the complaining creditors must have a lien is no longer law; and in any event in the case at bar the "Bondholders" were lienors. Mr. Glenn says that a third person cannot be "charged under the statute of fraudulent conveyances because the sole aim of that law is to nullify the grantee's title. The meddling outsider becomes liable under principles that are easy to understand, but they do not flow directly from the Statute of Elizabeth or any modern substitute." ** In the case at bar, even though Glass was one of those who took part in bringing about the conveyance of the property of "U.O.P.," and though he therefore did fulfil one of the conditions of liability, he would not be liable unless he had known that the securities of "M.S.P." which were offered for the "U.O.P." bonds were not an "equitable equivalent"; or unless he had been informed of facts from which a reasonable person would have supposed that they were not "equitable equivalent." Suppose the new bonds were not in fact such an equivalent for the old; certainly there is nothing in the record to show that Glass thought so, or that from what he knew a reasonable person would have thought so. On the contrary, the only evidence is that he and the reorganization com-

---

* *Adler* v. *Fenton*, 24 How. 407, 413; *Findlay* v. *McAllister*, 113 U. S. 104, 111, 114.

** Glenn, Fraudulent Conveyances, § 56.

mittee, which was more familiar with the facts than anyone else except perhaps Glass himself, thought that the exchange was of equivalents. Similarly, there was no evidence that "U.O.P." itself had that "intent to defraud" which is a condition of any fraudulent conveyance under the Statute of Elizabeth, except in cases where no fair consideration whatever passes to the grantor,* which was not the situation in the case at bar. "U.O.P." was at the time of the transfer in the custody of the court, whose special master, as directed by the decree, executed the conveyance of the Eureka shares and of the guaranty and intercorporate claims. The only persons whose intent could have been relevant to this conveyance were the reorganization committee itself and Glass, and the same considerations that we have just mentioned touching Glass apply equally to the committee. The judgment in favor of Glass will be affirmed, and *a fortiori* that against Tumulty.

It is not necessary to discuss at length the "Bondholders'" claim against "M.S.P." which was brought into the suit after they filed their motion in 1944 to compel the receivers to account. This claim is against "M.S.P." as grantee of "U.O.P.," on the theory that the sale was a fraudulent conveyance; and if there was no fraudulent intent there could be no recovery against even the grantee. Hence the same considerations that dispose of the claim against Glass personally on the merits dispose of that against "M.S.P." However, we cannot agree with the conclusion below that the "Bondholders'" claim is not barred by the New York Statute of Limitations under the doctrine of *Guaranty Trust Co.* v. *York*, 326 U. S. 99. The jurisdiction of the District Court depended solely upon diversity of citizenship, and the substantive rights and liabilities probably depended upon the law of the place where the

---

* Uniform Fraudulent Conveyances Act, § 4.

BLEED THROUGH POOR COPY

transfer was made; at any rate they depended upon the law of some state and not upon federal law. Although, as has appeared, the actual deed was made by a special master of the court under its direction, the "Bondholders" may not take the position that the transfer was illegal under federal law, for the court confirmed it and they did not appeal. They must argue that its validity depended upon the same state law that determines such a conveyance between individuals, and that the situation is as if "U.O.P." had made the conveyance in the course of a reorganization out of court, in which event the Statute of Limitations of New York would apply. Nor is it material that the final decree in the main action enjoined all creditors from bringing any action against "M.S.P." That did not toll the prosecution of its claims by the "Bondholders"; all it did was to compel them to assert their claims in the District Court. Again, it is not material that Glass and Tumulty, as receivers of the other corporations, had not been discharged. As we said at the outset, the "Bondholders" had no interest in the guaranty or the intercorporate claims after their sale to "M.S.P." Even if these had been sold at too low a price, they passed to "M.S.P." whose title to them would not thereafter be affected by anything done in this action. Hence the defence of the statute would be a bar, even if the claim had been proved.

In what we have just said, we do not forget what we said on the first appeal regarding the claim against the "Receivers"; nor do we wish in any way to throw doubt upon it. This was what we did say, so far as it is relevant here. "But we think that, with respect to the obligations of a receiver appointed by a federal court, the New York rule should not control. A claim against a derelict receiver is not against an ordinary trustee but against a court's officer. Who has the right to assert such a claim is a question affecting the integrity of the court itself. The

federal courts, in holding their own officers to accountability, should not be hampered by state court decisions relating to ordinary trustees. When the United States issues a check, rights in that check (despite Erie R. Co. v. Tompkins, 304 U. S. 64) 'are governed by federal rather than local law.' Clearfield Trust Co. v. United States, 318 U. S. 363, 366, 367. When a federal receiver incurs obligations through misconduct, the title thereto is, we think, similarly to be determined by 'federal law.'" Had the action been against the special master who conveyed the property to "M.S.P.," this language would have applied, just as it would have applied to Glass and Tumulty, had they "misconducted" themselves. But the "Bondholders" had no more claim against the special master than they had against Judge Knox of whom he was the instrument; and, to repeat, it is only on the theory that Judge Knox's order did not validate the conveyance, but left it as it would have been if the conveyance had been out of court, that any claim can exist. Hence, the state law must govern, including its Statute of Limitations. The judgment dismissing the claim against "M.S.P." must also be affirmed.

Judgment affirmed.

BLEED THROUGH POOR COPY

FRANK, *Circuit Judge,* dissenting (as to the liability of Glass):

My colleagues concede that if Glass, as receiver of UOP, violated his duty of undivided loyalty to any of the bondholders of that company, then he had the burden of proof as to most of the matters now before us, and that then many of Judge Smith's findings, favorable to Glass, do not stand up but are "clearly erroneous." My colleagues also concede, in effect, that whichever side in this litigation had that burden must lose the decision. I dissent primarily[1] because I think that Glass was not (as my colleagues say he was) "entirely innocent" and that he did violate that duty, in that he had undisclosed interests, adverse to the UOP bondholders, which might well have tended to influence him to further the interests of claimants junior in rank to those bondholders, with respect to the assets of UOP.

The court, in its decree of November 15, 1929, directing the foreclosure sale of the Eureka stock, found that there was due to the UOP bondholders, $4,500,000 (approximately), representing principal of about $2,500,000 and interest of about $2,000,000.[1a] So that UOP then owed each holder of a $1,000 UOP bond about $1,833. Each holder of such a bond, not deposited under the plan, received on July 25, 1933, as a result of those sales, $698.55 in cash, or about 39% of the amount due on November 15, 1929

---

1 I say "primarily," since (as will appear, *infra*) I think that, as to some important items, even if appellants had the burden of proof, they discharged it.

1a The holders of the UOP bonds were entitled to receive semi-annual payments at the rate of 8% plus so-called "interest participation" not exceeding 20¼% per annum.

The court, in its decree of November 15, 1929, stated that the overdue interest and "interest participation" (together with interest thereon) then came to approximately $2,000,000.

Omitting interest on interest, the figure was about $1,600,000.

(but without interest, on the amount thus paid, from that date to July 25, 1933). For reasons I shall state, I think Glass had the burden of proving that this recovery was not most inadequate and unfair.

1. *Applicable Principles*

As this case relates to the conduct of a receiver appointed by a federal court, and thus affects the integrity of the federal judicial process, I shall discuss that conduct in some detail. The discussion divides into two major categories: (a) The unfairness of the prices paid at the judicial sales for the UOP assets. (b) The unfairness of the reorganization plan.

It will be helpful, by way of prelude to such a discussion, to repeat these general principles stated in our former opinion (154 F. (2d) at 991-992) and with which my colleagues now express agreement: "A receiver, as 'an officer or arm of the court,' is a trustee with the highest kind of fiduciary obligations. He owes a duty of strict impartiality, of 'undivided loyalty,' to all persons interested in the receivership estate, and must not 'dilute' that loyalty. He is 'bound to act fairly and openly with respect to every aspect of the proceedings before the court. * * * The court, as well as all the interested parties,' have the 'right to expect that all its officers,' including the receiver, will not 'fail to reveal any pertinent information or use their official position for their own profit or to further the interests of themselves or any associates.'[2] A receiver has the 'affirmative duty to endeavor to realize the largest possible amount' for assets of the estate.[3] If he has vital information which, if disclosed, might bring a better price

2 *Crites, Inc.* v. *Prudential Company*, 322 U. S. 408; *Woods* v. *City Bank Company*, 312 U. S. 262, 263.

3 *Jackson* v. *Smith*, 254 U. S. 586, 588.

BLEED THROUGH POOR COPY

for property * * * sold pursuant to court order, he must fully disclose it 'prior to the sale when the prospects [are] greater for successful bargaining.'[4] Since failure to make such full disclosure has 'a tendency to dampen the sale,'[4a] it is presumed that it did so, where the receiver had an interest in the sale in conflict with that of any other parties to the proceeding, 'regardless of whether it actually had an adverse effect or not,' because 'the incidence of a particular conflict of interest can seldom be measured with any degree of certainty.'[5] A decree confirming such a sale does not exculpate the receiver.[6] When the receiver has brought about such a sale, and the property after the sale has been transferred to a company in which interests of innocent third persons have become vested, usually the sale will not be set aside if there is available the more practicable method of surcharging the receiver for the difference between the price paid and the value of the property.[7] Where a receiver has a possible personal interest adverse to those of any parties to the receivership, it is usually unwise for him to participate in the reorganization; if he does so, he must act with unusual caution. * * * A receiver who has strayed from his duty to the injury of anyone interested in the estate can and should be sur-

---

4 *Crites, Inc.* v. *Prudential Company, supra.*

4a *Ibid.*; cf. *Button* v. *Cities Fuel & Power Company*, 300 F. 280, 299, 301 (C. A. 4), cert. den. 266 U. S. 619; *Investment Registry* v. *Chicago & M. E. Ry. Co.*, 212 F. 594 (C. A. 7).

5 *Crites, Inc.* v. *Prudential Company, supra; Woods* v. *City Bank, supra; Jackson* v. *Smith, supra; cf.* as to trustees generally, *President & Directors of Manhattan Company* v. *Kelby*, 147 F. (2d) 465, 476 (C. A. 2); Restatement of Trusts, Sec. 170, comment c.

6 *Crites, Inc.* v. *Prudential Company, supra; cf. Pangburn* v. *American Vault, Safe & Lock Co.*, 205 Pa. 93, 54 Atl. 508, 510; *Gutterson & Gould* v. *Lebanon Iron & Steel Co.*, 151 F. 72, 76-77.

7 *Pangburn* v. *American Vault, Safe & Lock Company, supra; cf. Koontz* v. *Northern Bank*, 16 Wall. 196, 202-203.

charged when he asks approval of his final accounting.[8] The rule that a receiver must not be motivated by personal considerations is prophylactic; its sanction is a surcharge."[9] See also Restatement of Agency, Secs. 387, 389 and Comments c and e, Sec. 390 and Comments a and f; Mechem, Agency (2d ed. 1914) Secs. 1188 *et seq.;* the recent case of *Mosser* v. *Darrow,* 341 U. S. 267;[10] and the ancient authority, Matthew VI, 24: "No man can serve two masters: for either he will hate the one, and love the other; or else he will hold to the one, and despise the other."

2. *My colleagues' tacit, but untenable, key assumption, i.e., that a "system" reorganization was essential, and that a separate reorganization of UOP was impractical and not for the best interests of the UOP bondholders.*

Indispensable to all my colleagues' conclusions, and therefore to their decision, and to Judge Smith's, is an assumption which neither they nor he ever discuss but which they take for granted. I mean their tacit assumption that it was impractical to reorganize UOP separately—apart from the reorganization of the other companies in the MSO holding company "system"—and that the UOP creditors (namely the UOP bondholders) were not disadvantaged seriously by a unified or "system" reorganization, *i.e.,* one involving the creation of a single new company

8 *Crites, Inc.* v. *Prudential Company, supra.*

9 *Woods* v. *City Bank, supra; Weil* v. *Neary,* 278 U. S. 160, 173; *Crites* v. *Prudential Company, supra; Jackson* v. *Smith, supra; Magruder* v. *Drury,* 235 U. S. 106, 119, 120.

10 In an early case, it was said that a receiver is "the officer and representative of the court * * * and having in his character of receiver no personal interest but that arising out of his responsibility for the correct and faithful discharge of his duties." *Beverly* v. *Brooke,* 4 Gratt. 187, 208 (Va.).

BLEED THROUGH POOR COPY

owning or controlling all the assets of UOP as well as the assets of most of the other companies in receivership. If (as I think) that assumption is untenable, then the perspective becomes basically different. For then it appears that Glass had substantial personal interests (a) which would be realized through the consummation of the "system" reorganization that he furthered but (b) which would not be realized if UOP were separately reorganized. To make clear the fallacy of my colleagues' key assumption, I must briefly sketch the relation of UOP to MSO.

MSO, the top holding company, owned, directly and indirectly, the stock of UOP. In turn, UOP owned all the stock of Eureka, and Eureka owned some 82% of the stock of Turman. UOP had issued, and there were outstanding, about $2,400,000 of bonds secured by a pledge of the Eureka stock. Of course, the lien of these bonds on that stock (a first and only lien), and the claim of those bonds for any deficiency, were senior to any interest in the Eureka stock which could be asserted by MSO, the stockholder of UOP, or by stockholders or creditors of MSO (who were but stockholders, or creditors of the stockholder, of UOP). The UOP bondholders were virtually the sole creditors of UOP.

Eureka owned some 82% of the stock of Turman which owned the most valuable property of any company in the so-called holding company "system." So the receivers had stated in their reports filed in 1927 and 1928. The reorganization plan, dated July 29, 1929, said of Turman that "it is the most successful and owns the most productive properties of all" the receivership companies. Glass testified before Judge Smith that Turman was "really the most important [company] in the receivership."

The Supreme Court has recognized that the creation of a single new reorganized company, to take over properties theretofore separate, may be justified, but only

"where unified operations [by a new company] of separate properties [by such a single new company] are deemed advisable and essential." *Consolidated Rock Products Company* v. *Du Bois,* 312 U. S. 510, 530-531; cf. *National Bank* v. *Flershem,* 290 U. S. 408. Here such a single new company was not at all essential to, but, as we shall see, substantially harmed, the non-depositing bondholders of UOP. But never, so far as appears, did Glass propose, as an alternative to a "system" reorganization, the separate reorganization, by the UOP bondholders, of UOP. In the long trial leading to this appeal, he did nothing to show, and Judge Smith did not find, that such a separate UOP reorganization was impractical or not markedly more advantageous to UOP bondholders—as distinguished from MSO stockholders and MSO's other creditors—than the "system" reorganization which he recommended.

Such a separate reorganization could easily have been accomplished by a foreclosure sale of the Eureka stock, at which the UOP bondholders (with their huge claim for principal and unpaid interest) could have outbid anyone else. The earnings of Turman would have made it entirely feasible for such a separately reorganized UOP company to go it alone; the record contains nothing to indicate (nor does Glass argue) the contrary.[11] In this connection, it must not be overlooked that, as UOP receiver, Glass served as the fiduciary of all the UOP bondholders, not merely those who assented to the reorganization plan.

---

11 In a letter of October 27, 1927, Glass wrote that there were some of the companies in the "system" whose "only reason for being in receivership is the misfortune of having been connected with Middle States."

The "misfortune" of the UOP bondholders was that, because UOP had been "connected with Middle States," Glass did not give consideration to a plan for reorganizing it separately, since he had a personal interest in a "system" reorganization.

BLEED THROUGH POOR COPY

I shall discuss later, in detail, the judge's pressure for a reorganization. Here I note that never did the judge press for a "system" reorganization; nor did he ever approve the plan, after notice and hearing, as to its fairness. The provision of his order of October 3, 1924, appointing the receivers, that the receivers, during the receivership, should administer the properties of the several companies "as an entirety," was not, of course, a direction that a reorganization plan should deal similarly with those properties. Indeed, that very order of October 3, 1924, explicitly provided that the receivers should "keep and maintain all the properties and assets of the defendant companies separate and distinct from those of the other defendant companies, and do such things and preserve and keep such records as shall maintain and preserve separately at all times the identities of the respective properties of the respective defendant companies, and to open and keep separate books of accounts and records for each and every of the defendant companies so as to show at all times the separate business transactions of the separate defendant companies."

In the light of the foregoing, I now address myself to Glass' personal interests adverse to those of the UOP bondholders.

3. *Glass' undisclosed personal interest in a fee for services rendered in 1924 to the MSO stockholders' committee.*

Glass' career in these receiverships illuminates his conduct. That career began in 1924 when, in the court below, as lawyer for Shivers, a stockholder of MSO, in a stockholders' suit, he sought to have a receiver appointed for that company. Before the court took action in that suit, Phelan, a creditor of MSO—whom Glass did not represent—filed a bill, also in the court below, seeking a receivership of MSO. The court consolidated the Shivers and

Phelan suits, and appointed two receivers. Under an amended and supplemental bill, the same two men were also appointed receivers of UOP and of other companies in the so-called holding company "system," including UOP. In those proceedings, Glass represented a committee of MSO stockholders.

Subsequently, his firm was appointed counsel for the receivers of MSO, UOP and the other companies in receivership.[12] At that time his firm ceased to be counsel for the MSO stockholders' committee, and was succeeded by other lawyers representing it. Still later, on January 27, 1926, he became one of the receivers. For the four years, 1926-1929, he was paid, as receiver, fees of $175,000.[13]

But, during those years, he retained his interest in his firm's fee as lawyers for the MSO stockholders' committee, a fact not known to the receivership judge until Glass privately disclosed it to the judge—but *only* (on or about January 15, 1930) *after the confirmation of the judicial sales*, at a time when the judge declared he had no jurisdiction over such matters. In those circumstances, on the direction of the reorganization committee, Glass' firm was paid that fee, consisting of $15,000 in cash and voting trust certificates for 150 Class B shares of the new company.[14] This was not, as my colleagues suggest, compensation "trifling in value."

---

12 The firm ceased to be counsel for the receivers when Glass became a receiver. For these services, the firm received $67,500.

13 Thus he and his firm received from the receivership $242,500—aside from the fees paid for services to the MSO stockholders' committee and the share of Hamburg's fee.

14 Appellants say such was the fee. The record indicates that it was $19,999.99 in cash and the 150 shares.

BLEED THROUGH POOR COPY

Without a "system" reorganization, Glass could not have been paid this fee:

Everyone agrees that, at the time of the reorganization, MSO was insolvent and that there was no "equity" in its stock. Absent the reorganization, then, the MSO stockholders would have had nothing and the MSO stockholders' committee could have paid its lawyers nothing, for their fee was contingent upon a reorganization in which the MSO stockholders participated. But such participation depended on a "system" reorganization, *i.e.,* one owning or controlling most of the assets of the companies in the system and especially the Eureka stock which was essential to such a reorganization.

Thus Glass had a personal interest in bringing about such a reorganization. To achieve just that, he untiringly labored with the reorganization committee, "organized," so he reported in May 1928, "at the suggestion of the receivers." He wrote a letter, dated July 29, 1929, published in the reorganization plan, urging all securityholders to accept the plan.

The reorganization plan provided that the new company would assume payment of counsel for the several committees, including the MSO stockholders' committee, in such amounts as the reorganization committee approved. Because of his hearty cooperation with the reorganization committee, beyond possible doubt that committee was most friendly to Glass, and therefore most likely, if it became the purchaser at the judicial sales, to pay the fee of Glass' firm, as lawyers for the stockholders' committee.[15] It was, then, distinctly to his personal advantage to insure that the reorganization committee should be the successful bid-

15 One member of the reorganization committee was chairman of the MSO stockholders' committee which Glass had represented as lawyer in 1924.

der and that the reorganization plan—which provided that the new company would own the Eureka stock—should become effective.

Glass' cuttlefish argument.

Here Glass tries a cuttlefish argument: He says that, when, in 1924, his firm was succeeded by another firm (the "Cunningham" firm) as counsel for the MSO stockholders' committee, no arrangement was made to divide the fees; that Jackson, a member of the Cunningham firm, testified that this arrangement for splitting the fee was not made until January 1930; that Glass, on January 15, 1930, first learned "that it was proposed (by one of Glass' partners) to divide the fee to be paid to the Cunningham firm in lieu of separate fixation of fees for the services successively rendered by" Glass' firm "and the Cunningham firm as attorneys for the stockholders' committee"; and that Glass then—*i.e.*, about January 15, 1930—"informed the court of those facts." In so arguing, Glass does not deny the pivotal fact, *i.e.*, that, while acting as UOP receiver, he retained a personal interest in a claim for fees against the stockholders' committee,[16] which interest he did not reveal until he privately disclosed it to the court several weeks after the court confirmed the sales to the reorganization committee. All he then, belatedly, told the court was that he would obtain the fee by sharing in the Cunningham firm's fee instead of by a "separate fixation." How that tardy revelation of the fact exculpates him is incomprehensible.[17] The fact that he got his fee by sharing

16 He testified that his firm "had a potential interest in compensation for services we rendered to the stockholders' committee up to the time of our resignation" as counsel for that committee.

17 This comment applies to Judge Smith's equivocal finding: "Glass' firm, in lieu of separate fixing of fees for its services to the stockholders' committee in the early stages of the receivership prior to

BLEED THROUGH POOR COPY

contingent

in the Cunningham firm's fee is not the point. The point is that, as receiver, he had secretly retained a right to a fee from the stockholders' committee. See *Crites, Inc.* v. *Prudential Co.*, 322 U. S. 408, 416.

His retained and undisclosed interest in that fee should be compared with the statement in the receivers' reports, filed with the court in 1927 and 1928 and then mailed to many securityholders, that the receivers had "no personal interest in any company as against another."

My colleagues say, concerning this fee, that it did not give rise to any adverse personal interest in Glass because, before the sales, the amount of this fee was unliquidated. But that very fact underscores the existence—and the vice—of this adverse interest: The fee was paid only after the "system" reorganization plan became effective, and would not have been paid otherwise. It was compensation "dependent upon a particular bidder being successful." See *Crites, Inc.* v. *Prudential Co.*, 322 U. S. 408, 416. Surely such an interest was not "remote or speculative." (See discussion, *infra*, in point 5.)

4. *Glass' personal interest in Hamburg's fee.*

In August 1926, Hamburg, together with his associates, Ausberry and Barton, applied for an interim allowance of $10,000 for services in connection with the receivership tax matters. On August 25, 1926, Glass wrote the receivership judge a private letter (not made part of the court records) stating that he wanted the judge to know, before he acted on this application, that there was "an arrangement whereby

---

its appointment as one of counsel for the receivers, shares in the allowances to Moore, Hall, Swan & Cunningham, having first brought the arrangement to the attention of the court."

Note that Judge Smith did not find that, before confirmation of the sales, Glass brought to the attention of the court any claim by his firm for fees as counsel for the stockholders' committee.

my firm has an interest in all his [Hamburg's] business in return for rent, office accommodations and services and business referred to him."

More than three years later, on December 23, 1929, just before confirmation of the sales, Hamburg applied in open court for a final allowance. Glass, who was present, did not then state to the court that this "arrangement" had continued and was still operative. Later, on February 4, 1930, about six weeks after confirmation of the sales,[18] Glass wrote the receivership judge a letter (not made part of the court records), reminding him of the 1926 letter, and saying "this interest continues at this time." Hamburg received a final allowance of apparently $62,500 in which Glass shared (in an amount not disclosed).

The fact that Glass felt the need of writing this letter of February 4, 1930, to remind the judge of the 1926 letter, goes to show that the judge, before he confirmed the sales in December 1929, did not know that Glass had a continuing interest in Hamburg's fee.[19] Since the judge had no such knowledge at that time, we have another instance of Glass' personal interest tending adversely to affect his loyalty as receiver. For a receiver, unburdened by conflicting inter-

---

18 Glass refers to the fact that, between 1926 and 1929, Hamburg had received interim allowances in addition to the $10,000 allowance made to him in 1926. The fact that Glass, in 1930, called the judge's attention to his 1926 letter, and to no intervening letter, goes to show that, when the judge made interim allowances to Hamburg between 1926 and 1930, Glass had not told him that his interest in Hamburg's fees then continued.

The record contains no evidence to support Judge Smith's finding that Glass had brought to the court's attention the arrangement with Hamburg "prior to each application for allowance." Indeed, Glass testified that he drew Judge Knox's attention to this arrangement "upon the first application for an allowance" (*i.e.*, in 1926) and that "before any order was signed on his application for a final allowance" (after confirmation of the sales), "I referred him to my original letter and reminded him of my interest in the matter."

19 The court ordered confirmation on December 24, 1929.

BLEED THROUGH POOR COPY

ests, might have felt it necessary to suggest to the court reorganization of UOP separately. But Glass, as a beneficiary of Hamburg's potential award, was interested in effecting a plan whereby all of the assets from which the award would be paid would be in hands not likely to oppose the claim, *i.e.*, a "system" reorganization in which control was exercised by persons friendly to Glass. Perhaps Glass' stake in the Hamburg claim was insufficient to influence his judgment in respect of so major a question; but the very possibility of conflict created, at a minimum, the duty of the very fullest disclosure to the judge before confirmation of the sales—a duty Glass did not perform. *Crites, Inc.* v. *Prudential Co.*, 322 U. S. 408, 416.

5. *Glass' undisclosed expectation of becoming lawyer for the reorganized company.*

Before the confirmation of the sales, Glass had rejected suggestions by the reorganizers that he become president of the new company. He did accept that post after the reorganization; but I agree with my colleagues that, on the evidence and the findings of Judge Smith, any expectation of becoming president cannot be considered as motivating Glass' conduct.

My colleagues, however, concede that, long before the judicial sales, Glass had "quite frankly declared" that he would like to be "lawyer for the reorganized company." [19a] Since the reorganizers were eager to have him as president, it goes without saying that Glass knew that the reorganizers

19a He so wrote in letters, dated October 27, 1927, in which he stated he thought that, fairly soon, a reorganization "can be worked out." In one reply, the writer said, "I assume, of course, that your services in a legal way will be engaged by the new corporation." In another reply, another writer said, "You should be retained in a legal capacity, as the reorganized company would then have the benefit of your good judgment on legal matters and all questions of policy."

would satisfy his desire to attain the less important position of lawyer for the new company. Therefore he had far more than a mere "hope": His selection as lawyer did not (as my colleagues say it did) depend on what the "administration" of the new company "might decide." For he had a virtual assurance from the reorganizers that the new company would choose him. To be sure, this assurance could not be carried out unless the reorganization committee became the successful bidder at the judicial sales. But that contingency cannot obliterate the fact that Glass had an interest in conflict with his duty of undivided loyalty.[19b] This interest was not disclosed to the receivership judge.

My colleagues say that this interest was "too remote," "too feeble an inducement to be a determining motive." That might have been true if a "system" reorganization had been essential, since then perhaps it would have done the UOP bondholders no harm to have Glass aid such a reorganization; in such circumstances, perhaps it could have been said that this motive would not appreciably deflect his loyalty to them.[19c] But, since a "system" reorganization was not essential, that motive may well have counted heavily in influencing him to plump for such a reorganization as against a separate reorganization of UOP. It is this factor, neglected by my colleagues, which renders inapposite the cases they cite.

In *Bullivant* v. *First National Bank*, 246 Mass. 324, the plaintiff, president of a failing corporation, entrusted his

19b *Cf.* Restatement of Trusts, Sec. 170, Comment e: "If the trustee sells to a third person for the purpose of repurchasing the property from the third person, although at the time he has no understanding with the third person as to the repurchase, he commits a breach of trust, and if he subsequently reacquires the property, he can be compelled to hold it subject to the trust."

19c I say "perhaps," because this particular "system" reorganization, which Glass furthered, gave participation to MSO stockholders. See point 14 of this opinion, *infra*.

BLEED THROUGH POOR COPY

shares in the corporation to the defendant, a creditor of the corporation, and agreed (subject to minor limitations) that the bank, as voting trustee of the shares, would have full ownership rights in them for three years. The plaintiff then sought, in derogation of that agreement, to enjoin the bank from voting the stock in favor of a proposed plan of reorganization, on the ground of conflict between the bank's interest as trustee and as creditor. The injunction was denied, for the bank was a creditor at the time of the agreement—a fact which was then surely known to the plaintiff—so that the bank's dual interest was created by the beneficiary and not concealed from him.

In *Anderson* v. *Bean,* 272 Mass. 432, the trustee owned approximately half of the shares of a corporation in his own right and the other half as trustee. He sold a part of his trusteeship holdings, and thus put his personal holdings in a dominant voting position. The beneficiaries sought to surcharge him. The court found that the new arrangement was of "no harm to the trust" and "no profit to the trustee." Perhaps the court was wrong in believing there was no advantage to the trustee; but the relevant fact, for present purposes, is that the court thought there was no advantage, and therefore an inquiry, into whether his actions were influenced by hope of private gain, would have been meaningless.

In *In re Harton's Estate,* 331 Pa. 507, and in *Pike* v. *Camden Trust Co.,* 128 N. J. Eq. 414, a trust company, which took over mortgages and allotted participation certificates to trust estates administered by it, also acted as rental agent for the mortgagor, and its commission as agent was deducted from distributions of income to the participating certificate-holders. The courts in each of these cases held there was no conflict of interests, and that a trustee may be compensated for a service performed as part of the administration of the trust estate.

These two cases reflect a recent tendency toward relaxing the strict rule that a trustee may not employ himself because, in so doing, "he cannot perform one part of his trust, namely, that of seeing that no improper charges are made." See *Broughton* v. *Broughton*, 5 DeGex, M. & G. 160; *Gray* v. *Robertson*, 174 Ill. 242, 51 N. E. 248. Bogert, to whom relaxation of the rule is apparently distasteful, explains the relaxation on the ground that the court is confronted with a situation in which a service has already been performed for the estate and that to deny the award would unjustly enrich the estate. 3 Bogert, Trusts 142. Whatever the reason, however, the conflict of interests created by a trustee employing himself as lawyer, rental agent, or whatever, can affect his judgment in only one small matter, *i.e.*, passing on the award to be made to himself for the service rendered, while the conflict of interests in Glass' situation might have affected his judgment in respect of major matters.

In *Dabney* v. *Chase National Bank*, 196 F. (2d) 668 (C. A. 2), there was only a possibility of a conflict of interest dependent upon a series of unlikely contingencies which, in fact, did not come about. In the instant case, the conflict depended on only one contingency—a system reorganization—and the trustee, far from leaving the contingency to chance, was active in bringing it about.

My colleagues quote a short excerpt from a passage in our opinion in *York* v. *Guaranty Trust Company*, 143 F. (2d) 503, 514 (C. A. 2). I think the entire passage, reading as follows, states the applicable rule: "Of course, the courts should not impose impractical obligations on a trustee. Merely vague or remote possible selfish advantages to a trustee are not sufficient to prove such an adverse interest as to bring his conduct into question. But here the advantages seem not to have been thus vague or remote. That a trustee owes his beneficiaries undivided loyalty entirely un-

BLEED THROUGH POOR COPY

tinged by considerations of any important benefits to himself is an old truth, and one whose edge cannot be dulled by frequent use. If the trustee here allowed its judgment to be affected by any such factors, it acted improperly. Cf. *Pepper* v. *Litton*, 308 U. S. 295, 311, 60 S. Ct. 238. If it failed to exercise the powers it held in trust because it entertained a belief that such inaction might be to its own substantial benefit (while failing to consider the consequent harm to any of its beneficiaries), then it breached its obligations, regardless of whether its belief, objectively viewed, was illusory. That is to say, the trustee should be held liable, if the trial court reasonably infers from the evidence at the trial that the trustee, in making its decision, was moved to do so in any degree by the thought that it might incidentally secure a substantial advantage to itself. In such circumstances, nothing would turn on the fact that the trustee did not in fact derive benefits, if its inactivity caused loss to any of its beneficiaries."

Glass cites *Acker* v. *Hamilton*, 85 F. (2d) 574, 576 (App. D. C.) as if the court there had held that an "expectant relationship" does not suffice to create a conflicting interest. There, pursuant to statute, the Comptroller of the Currency took charge of a bank and determined that it was insolvent. Stockholders, who were assessed on their bank stock, complained that a sale to another bank by the Conservator, who had been appointed by the Comptroller, was unfair (and resulted in a large deficiency). They argued that, before the sale, the Conservator had been designated as vice-president of the purchasing bank and, after the purchase, was actually elected to that position. The court said: (1) "The sale realized the full present market value" of the assets sold. (2) The Comptroller had arranged the sale, and the Conservator "served only as a medium through which the scheme of salvage was affected. Here there was neither occasion nor opportunity for the Conservator of this

bank to consult his private interests. He acted as the mouthpiece or agent of the Comptroller. The sale, therefore, was the Comptroller's sale, and it is obvious the Conservator neither had nor could have any private interests to serve." (3) The Conservator's designation as vice-president "was not secret and was commonly known." All these circumstances, the court said, must "qualify" the usual rule regarding fiduciaries "to the extent that something more than an expectant relationship ought to be shown before a transaction should be condemned and set aside which is fair and equitable in all respects—and in which the Conservator acted only by authority of his superior." Plainly, if the numerous qualifying facts, stated by the court, had been absent, it would have held the other way.

6. *Glass favored the junior interests at the expense of the UOP bonds.*

During the receivership, not one cent of interest on the UOP bonds was paid. Glass explains this fact thus: By October 1929, this unpaid interest (with interest thereon) aggregated about $1,725,000. Payment of this huge sum (says Glass) was impossible, since the sole means by which the necessary funds could have been obtained was payment of dividends by Turman to Eureka, and Turman was in such financial condition that it could not have paid out $1,725,000.

But that is not the question. The question is whether not all but some ponderable part of that interest could have been paid. Had it been, then, just to that extent, the UOP bondholders would have benefited. But, just to that extent MSO stockholders and creditors would have been disadvantaged, and the achievement of a "system" reorganization would probably have been frustrated. This appears from the statement to the court, on March 9, 1929, of

BLEED THROUGH POOR COPY

Lehman, the lawyer for certain creditors of MSO (the MSO Serial Noteholders' Committee) that the receivers "have been using the money, which should go to the [UOP] bondholders, for the purpose of improving the property for the benefit of all the securityholders of Middle States Oil Corporation" including its stockholders. Glass here favored the MSO stockholders and aided the "system" reorganization in which he had a personal stake.

There is evidence—in addition to Lehman's candid statement, undisputed by Glass who was present at the time—that it was possible, long before the sales, to pay some considerable part of the overdue interest:

(a) Judge Smith found, "In the early stages of the receivership, an attempt had been made [in the so-called Manning suit] to obtain a domiciliary receivership in Delaware which had been defeated primarily on the basis of testimony by Glass who had become one of the [federal court] receivers that the companies were solvent in the sense that they either had or could obtain whatever funds were needed to meet their admitted obligations." In that Delaware suit, Glass testified that one of the ways to meet those obligations was by his causing subsidiary companies to declare and pay dividends. At the trial before Judge Smith, Glass endeavored to explain away this testimony. Judge Smith found that Glass was "unconvincing" in "his testimony as to the meaning of his statements in the Manning trial in Delaware."

(b) As Judge Smith also found, the receivers, for other purposes, caused MSO to borrow money from subsidiaries for acquisition of property or to discharge debts. As already noted, the principal oil production and revenues of the receivership companies derived from the properties in the Seminole field, owned by Turman. In their report to the court on May 7, 1928, the receivers stated that, by reason

of the Seminole development, the position of the Middle States companies had greatly improved and that "claims against the companies, $1,808,033.93, have actually been paid off out of income during receivership." [20] Yet not a cent went to pay any of the interest on the UOP bonds.

(c) Glass now argues that, until the beginning of 1928, when the matter was settled, there was litigation affecting the title of Eureka to 30% of the Turman stock. But, even so, this left Eureka, before 1928, with about 52% of Turman stock not in dispute, so that apparently Eureka could have caused Turman to declare substantial cash dividends which could then have been used, in large part, to pay United bond interest. Moreover, when the dispute re the Turman stock was settled, Eureka then held, undisputed, 82% of the Turman stock.[21]

Judge Smith made no finding on the subject of the ability, during the receivership and months before the judicial sales, to pay a substantial portion of the interest. He found merely that, at the time of the order directing those sales —*i.e.*, November 1929—United could not "have continued [*sic*][22] to pay the interest on the bonds." This is not a

---

20 In their report of May 7, 1928, the receivers also said that, during the latter part of 1929, they had commenced a "policy" of buying oil acreage and continued, "Up to the time when creditors were provided for, the receivers could not make any such purchases without possible detriment to creditors' interest. They, however, now feel that, when creditors have been fully provided for, they will best serve the interests of the stockholders by conservative purchases of well-chosen acreage in order to insure future production and income for these companies."

21 Glass testified before Judge Smith that it was "theoretically possible" for him to cause Turman (by a reduction of its capital stock) to declare a substantial dividend which could have been used to pay some of the UOP interest. He did not explain why it was not practically possible.

22 None had been paid since 1924.

BLEED THROUGH POOR COPY

finding that UOP could not have paid some considerable segment of the overdue interest long before that date. Significantly, my colleagues do not discuss this question.

Even if it be assumed that, on this issue, the appellants had the proof-burden, I think they discharged it. If, because of his selfish interest, Glass had that burden, he did not discharge it.

Appellants make a more sweeping contention. They argue that, all other factors aside, Glass' conduct with reference to the non-payment of interest was alone enough to put on him the burden of proof as to all phases of the case. Answering this argument, my colleagues take this position: The court, since it appointed Glass receiver of both MSO and UOP, necessarily put him in a position where, if any conflict arose between UOP interests and MSO interests, he had the implied authority—indeed the implied duty—to decide that conflict according to his own best judgment. If, say my colleagues, he decided adversely to UOP interests, and did so erroneously, he was liable to the UOP bondholders, but the burden of proving the extent of the loss was on them, since an erroneous decision involved no deviation from his undivided-loyalty duty because the court, by impliedly imposing on him the authority to make such a decision, relieved him of that duty.

In taking this position, I think my colleagues overlook the following: The cases hold that a trustee's duty of undivided loyalty is breached not only when he is (or might be) motivated by his own self-interest but also where he acts in the interest of any third person; and the cases also hold that one who is a trustee of two trusts, if he engages in dealings between the trusts, is guilty of disloyalty to one or the other, unless he shows that the transaction is fair to both, and that his duty requires him, in cases of doubt concerning such a conflict, either to resign as trustee of one of the trusts, or to refrain from acting until he has obtained the

instructions of a court.[23] Thus the Restatement of Trusts, §170, states: "The trustee is under a duty to the beneficiary to administer the trust solely in the interest of the beneficiary," and adds the following comments on that rule: "p. *Action in the interest of a third person.* The trustee is under a duty to the beneficiary in administering the trust not to be guided by the interest of any third person. Thus, it is improper for the trustee to sell trust property to a third person for the purpose of benefiting the third person rather than the trust estate. q. *Duty of trustee under separate trusts.* Where the trustee is trustee of two trusts, if he enters into a transaction involving dealing between the two trusts, he must justify the transaction as being fair to each trust. If the circumstances are such that the interests of the beneficiaries of the different trusts are so conflicting that the trustee cannot deal fairly with respect to both trusts, he cannot properly act without applying to the court for instructions." See, e.g., *Mosser* v. *Darrow*, 341 U. S. 267; *Detroit Trust Company* v. *Mason*, 309 Mich. 281, 306; *In re Sedgwick's Will*, 74 Ohio App. 444, 59 N. E. (2d) 616, 624 (Ohio); cf. *Berner* v. *Equitable Office Building Corp.*, 175 F. (2d) 218, 221 (C. A. 2). In the case of a receiver, receipt of such judicial instructions has been uniformly required. See, e.g., *Northern Finance Corp.* v. *Byrnes*, 5 F. (2d) 11, 12-13 (C. A. 8).[24]

---

23 Judge Smith said: "Some of Glass' transactions may have been harmful to some of the receivership estates. * * * It may be * * * he was unconsciously influenced by a desire to benefit the group of receiverships as a whole" rather than to act solely "for the benefit of any one of them. * * * That was a danger incurred by the court in order to avoid the expense of some thirty-eight additional receiverships." But Judge Smith added, "If it did occur and cause damage" to a particular estate, "some means must be found to rectify it."

24 In *Mosser* v. *Darrow*, 341 U. S. 267, 273-274, the court said: "It is argued, and the court of appeals appears to have been impressed by the argument, that this surcharge creates a very heavy liability upon a man who enjoyed no personal profit and must be condoned

BLEED THROUGH POOR COPY

The receivers did not seek or obtain the instructions of the court in respect of non-payment of the interest. True, in March 1928, and again in March 1929, others brought ~~this~~ the non-payment fact to the court's attention, and the court did not then order that any part of the overdue interest be paid. But I incline to doubt whether the court's failure to enter such an order amounts to an instruction or to a ratification of the receivers' previous inaction.

7. *Effect of Glass' personal interests: He had the burden of proof.*

At any rate, disregarding the facts just narrated in point 6, those discussed in points 3 and 5, *supra*,[25] suffice, I think, to put the burden of proof on Glass.[25a] If so, Judge Smith's findings of fact, so far as favorable to Glass, crumble—*i.e.*, cannot be held not "clearly erroneous"—since he rested them on his legal conclusions that (a) Glass had not violated his loyalty-duty and therefore (b) did not have the burden of proof.

My colleagues virtually admit that, if Glass had that burden, there is a lack of foundation for their ruling as to the fairness of the prices bid at the sales, and in particular, the price of the Eureka stock.

'so as not to strike terror into mankind acting for the benefit of others and not for their own.' 184 F. (2d) 1, 8. Trustees are often obliged to make difficult business judgments, and the best that disinterested judgment can accomplish with foresight may be open to serious criticism by obstreperous creditors aided by hindsight. Courts are quite likely to protect trustees against heavy liabilities for disinterested mistakes in business judgment. But a trusteeship is serious business and is not to be undertaken lightly or so discharged. The most effective sanction for good administration is personal liability for the consequences of forbidden acts, and there are ways by which a trustee may effectively protect himself against personal liability."

25 And probably also in point 4, *supra*.

25a *Cf.*, as to burden of proof, Restatement of Agency, Sec. 389 and Comment e, Sec. 390 and Comment f.

Glass delay and the loss of evidence.

Before I go further, I think it ~~wise~~ well to bring out a feature of this case which emphasizes Glass' burden of proof: Glass delayed filing his final account, and seeking discharge, as receiver of UOP, from the time of the confirmation of the judicial sales, at the close of 1929, until 1945 (and he then filed that account only after appellants procured an order directing him to do so). Some part of that delay is understandable. But why he waited fifteen years, Glass has never explained. Yet he asserts that he has been harmed because, during those fifteen years, documentary evidence has been lost and important witnesses have died. Surely this is a shoe-on-the-wrong-foot argument: The harm is to appellants. (*Cf.* the discussion of delays in *Southern Pacific Company* v. *Bogert*, 250 U. S. 483, and *Northern Pacific Ry.* v. *Boyd*, 228 U. S. 482.) Glass has put this court in a position where it must look at the facts as through a glass darkly:[26] Thanks to this delay, this case is one of the most complicated our court has ever encountered; we have devoted many months to a study of the record. (I disagree with some of the findings of Judge Smith, who was not the receivership judge, but, considering the complexities, that he made some mistakes of fact is not surprising; and I join my colleagues in criticizing that part of appellants' brief which imputes to Judge Smith a partiality in favor of the receivers.)

In 1944, appellants asked Glass, as receiver, for information concerning UOP. He refused this request. In 1945 they made a motion that they be allowed access to important receivership papers, never filed as part of the court's records but which Glass had in his possession; Glass filed an affidavit in opposition, in which he astonishingly referred to "the danger" of making such information available to

26 See 1 Corinthians 13:11-12.

BLEED THROUGH POOR COPY

them.[27] Judge Smith said that there was "a number of instances of impatience of Glass with requests for full information," and that because of "his reluctance to make full disclosures," Glass had no "cause * * * to complain about the burdens to which he has been put by reason of objectants' [appellants'] attempts to develop the full story which the objectants believed would substantiate their suspicions of wrongdoing. * * * The delay [in filing his final account] alone would give some basis for objectants' suspicions."

Concerning this delay, Judge Smith added: "His duty to the court, so long as any of the receiverships remained open, was to complete the work * * * of winding up the affairs of all the estates so that any minorities which had any surviving interest might have an opportunity to be heard on his discharge from his receivership duties."[28] Much in point, then, are these remarks of the Supreme Court in *Mosser* v. *Darrow*, 341 U. S. 267, 274-275, concerning a bankruptcy trustee: "A further remedy of a trustee for limiting, not avoiding, personal liability, is to account at prompt intervals, which puts upon objectors the burden of raising their objections. * * * It hardly lies in the mouth of a trustee to allow his liabilities to accumulate over such a period of time and then ask the court to relieve him of them because they have become too burdensome." Cf. *Matter of Hubbell*, 302 N. Y. 246, 254.

Our decision, in 1946, directed a full hearing on appellants' objections to Glass' discharge. In the long resultant trial before Judge Smith, there became known, for the first time, the facts concerning Glass' personal interests, adverse to the UOP bondholders, which could not have been ascertained from a search of the court's records or files.

---

27 See our earlier opinion, 154 F. (2d) at 990.

28 The interim accountings, from 1924 until 1945, were meager and uninformative.

8. *Glass abandons neutrality: He helps to bring about forced sales at prices tailored to a "system" reorganization, in violation of the doctrine of First National Bank* v. *Flershem,* 290 U. S. 504.

As a receiver, Glass had no obligation to help in the formulation and consummation of a reorganization of any of the companies in receivership; and, insofar as he did participate in such an effort, his duty was to remain neutral, as among the several interests. But, as above pointed out, Glass assiduously sought to accomplish a "system" reorganization; and the evidence reveals that a reorganization of the other companies, not including UOP, would have been decidedly less desirable from the point of view of the interest junior to the UOP bonds, as distinguished from that of the holders of those bonds. Remembering that Glass had come into this story initially as representative of those junior interests, and that he would profit personally from a "system" reorganization, it is not difficult to understand why he persistently pushed for such a reorganization.

First National Bank v. *Flershem,* 290 U. S. 504, shows how such a dominant purpose to preserve a "system" as an "entirety" could well work injustice to the non-assenting UOP bondholders. It teaches that, except in the case of a railroad or the like, a "unitary" reorganization should be regarded with marked suspicion.

The attitude of Glass and the reorganization committee towards non-depositors sheds light on their arbitrary method of picking the prices to be paid at the judicial sales:

(a) Judge Smith said of "the receivers and reorganizers," "They may have, and probably did, as was normal in those days, desired to effect a reorganization to be controlled by those interests represented on the reorganization committee." Whether that was "normal" practice in 1929 is questionable. But, even if it was then the usual practice,

BLEED THROUGH POOR COPY

that fact cannot serve as a defense. For in *First National Bank* v. *Flershem*, 290 U. S. 504 (1934), the court overturned such a practice adopted in a reorganization consummated in 1931. If this were a suit against the members of the reorganization committee for damages, perhaps their good faith belief in the normality of their methods would be pertinent. But that defense is not open to Glass, a receiver who had a personal interest in promoting a reorganization which disregarded the welfare of non-depositing UOP bondholders who were not "represented on the reorganization committee" but whom Glass did represent.

(b) Arkush, the lawyer consulted by Glass and the reorganization committee as a reorganization expert, testified that Glass and the committee chose, as the sales prices, 66⅔% of what they estimated as the "going-concern value" of each of the properties. Asked why they picked 66⅔%, he answered that that was then the conventional percentage used in connection with reorganizations, in order to make acceptance of a plan more attractive than the amount of cash payable to a non-depositor. That percentage was therefore purely arbitrary. In agreeing to those prices, Glass agreed that, as it turned out, the non-depositing UOP bondholders should receive in cash but approximately 69.8% of the face of their bonds and ~~but~~ 39% of the amount due them for principal and unpaid interest. (Even that amount of cash was not payable until about 3½ years after the effective date of the plan and then without interest for those years.)

The method here used of fixing judicial sales prices—tailored to a "system" reorganization plan—was condemned in *National Bank* v. *Flershem*, 290 U. S. 504.[29] The court made it plain that the prices paid at a judicial sale in such

---

29 We quoted from and applied the doctrine of that case in *In re N. Y., N. H. & H. R. Co.*, 147 F. (2d) 40, 49 (C. A. 2).

circumstances are not to be considered the same as prices at the usual "forced sale." The court said that, as the aim should be "to secure for non-assenting creditors the largest possible sum in cash," it was error "to treat the receivers' sale as merely a necessary step in effectuating the plan of reorganization."

9. *Glass' tainted advice vitiates the order confirming the sales.*

It is suggested that the prices agreed upon by the reorganization committee with Glass' concurrence, were, in effect, "upset prices." But an "upset price" is one determined by the court before the sale, after notice and hearing to all interested persons. It could be "a weapon with which the court" is able to "bargain with the committee," by insuring that the property will not be sold at too low a figure from the point of view of those not assenting to the plan.[30] Here the reorganizers, with Glass' approval, deliberately decided not to ask the court to fix upset prices—and the court did not fix them.

Glass argues that, before the sales, the receivership judge—in private, but it noted, not in open court—had been informed by Glass and the committees of the details of the reorganization plan; that consequently, in confirming the sales, the judge impliedly approved the plan; and that the judge thus acted on full information, when, by confirmation, he approved the prices, which therefore must be deemed to have been informedly adjudicated as fair. To this argument, there are several answers:

(a) Any receivership court properly regards its receiver as its eyes and ears. In this case, to more than the usual degree, the receivership judge leaned on Glass' ad-

30 6 Collier, Bankruptcy (12th ed. 1947) 41.

BLEED THROUGH POOR COPY

vice—and Glass had helped to fix the prices. But the judge did not know, before the sales' confirmation, that this advice was tainted, *i.e.*, that Glass had personal interests, then undisclosed to the judge, contingent upon the consummation of the reorganization plan via the judicial sales at the prices agreed upon by Glass and the reorganization committee. On account of this taint, Glass cannot hide behind the confirmation of the sales.[31]

Glass makes much of the fact that the judge, on his own initiative, asked for and received (in private) the independent judgment as to values of Cannon, an assistant to the receivers. But Cannon—who, before the receiverships, had been president of MSO—in replying to the judge, frankly stated that he was interested "in behalf of the MSO stockholders." Moreover, he said that if all the assets of UOP were sold, the UOP stockholders would receive the face amount of their bonds.

(b) *The court deviated from "standard practice" by not holding a hearing, on notice, as to the plan's fairness:*

The reorganization committee, after carefully canvassing the question, deliberately decided, with Glass' concurrence, not to ask the court, after a hearing, to pass on the fairness of the plan,[32] and the court explicitly stated that it refrained from doing so.

Glass argues that in 1929 it was not the practice in such receiverships for the court to hold a hearing, on notice to all interested persons, and then to pass on a plan's

---

31 See, e.g., *Matter of Hubbell*, 302 N. Y. 246, 253; *In re Trust Created By Will Of Enger*, 225 Minn. 229, 239-241 and cases there cited.

32 On the hearing on confirmation of the sales, the counsel for the reorganization committee said he was submitting a proposed order of confirmation. The court asked, "This includes the approval of the reorganization plan, does it not, or * * *" and was interrupted by counsel who said, "The reorganization plan as such is not submitted to the court for its approval. * * *"

fairness. I cannot agree. The *Boyd* case, 228 U. S. 482, had been decided in 1913. As a result, in the Missouri-Pacific reorganization in 1916—thirteen years before confirmation of the sales in the instant case—the decree provided that the court, in advance of the foreclosure decree, would, after notice, hear complaints as to the fairness of the plan's offers to various named classes of creditors, including bondholders.[33] With minor variations, this became the "standard practice."[34]

In 1926, in the important receivership-reorganization of the industrial, Wilson & Company, Inc.,[35] in the federal district court for the Southern District of New York—the very court in which the receiverships of UOP and MSO were then being administered—Judge Bondy, in the decree of sale, entered January 23, 1926, provided that, on February 11, 1926, before the sale, he would hold a hearing on complaints by interested persons as to whether the offers to creditors and securityholders, set forth in the reorganization plan, were fair, timely and equitable. He held such a hearing, at which no one appeared and complained. On February 13, 1926, before the sale, he entered an order that the offers were fair, timely and equitable. At the sale, on February 26, the successful bidder was the reorganization committee; and the judge confirmed the sale on the same day.

In December 1927—two years before confirmation of the sales in the instant case—there appeared in 27 Col. L. Rev. 901, an article by Swaine (a leading reorganization lawyer) which reported that, in all cases of railroad re-

---

33 This practice was begun in the Frisco Railroad reorganization in 1916. See Swaine, The Cravath Firm (1948) II, 172.

34 *Ibid.*, 172, 184, 186.

35 *John Eiszener Company* v. *Wilson & Co., Inc.*, U. S. District Court, Southern District of New York, in Equity, No. E 30-119.

BLEED THROUGH POOR COPY

organizations and in many cases of public utility and industrial reorganizations, the federal courts, after the Missouri-Pacific reorganization, had employed (indeed improved upon) the method there employed.[35a] Doubtless, this practice, well-established by 1929, was known to Arkush, the reorganization specialist, and was communicated by him to Glass and the reorganization committee who asked and acted upon his advice.[36] The outstanding fact here is that, with Glass' assent, the fairness of the plan was not considered by the court after notice and a hearing thereon.

The indenture trustee and Glass' tainted advice.

Glass argues that the acquiescence in the confirmation by the indenture trustee, under the indenture securing the UOP bonds, bound all the holders of the undeposited UOP bonds. But, since the indenture trustee justifiably relied upon Glass' views, and since they were tainted by his self-interest, Glass cannot use that acquiescence to shield him from liability to holders of undeposited bonds. Moreover, when a receiver has an interest conflicting with

---

35a In the reorganization receivership of *J. Z. Horter Co.* v. *Punta Alegra Sugar Company*, In Equity, No. E-54-44, pending in the court below, in 1932, the court held a hearing, on notice to all interested persons, as to the fairness of the plan; then found the plan fair; and thereafter ordered and confirmed the sale.

36 That it was so known to him, and that he did communicate it, appears from the following: A memo by Arkush, dated September 20, 1929, discusses the alternatives of submission of the plan for "judicial approval" before, or at, or after, entry of final decree. It states, "The most practical plan would be to submit Plan at time of decree or after decree and before sale, with notice of hearing on Plan, if required, to run concurrently with published notice of sale."

A memo of matters considered and decided at a meeting of counsel for the reorganization committee and Glass on September 23, 1929 (three days after the date of the Arkush memo) states that the draft of final decree was not to mention upset prices or the Plan and that the Plan was not to be submitted at that time.

his undivided-loyalty obligation, confirmation of a sale does not exculpate him. *Crites, Inc.* v. *Prudential Company*, 322 U. S. 408; *Woods* v. *City Bank*, 312 U. S. 262; cf. *President & Directors of Manhattan Co.* v. *Kelby*, 147 F. (2d) 465, 476 (C. A. 2); Restatement of Trusts, Sec. 170, Comment c.

10. *Unfair price paid for Eureka stock.*

Glass' basic argument, which my colleagues adopt, is (a) that Judge Smith found that the price paid for the Eureka stock was fair, and (b) that therefore any misconduct by Glass with respect to the sale of that stock is immaterial. I think that Judge Smith's finding is "clearly erroneous," even if appellants had the burden of proof, and especially so if Glass had it.

The reorganization committee, with Glass' approval, agreed that the committee at the sale should pay for the Eureka stock, and it did, $1,450,000. This figure, as above noted, was ⅔ of what the committee said it believed to be the fair going-concern value of that stock. Their going-concern valuation, on that basis, was therefore $2,175.000. In finding—some twenty-two years after the sales—that $1,450,000 was a fair price, Judge Smith used several tests. As my colleagues, however, employ but two of those tests, I shall discuss them only.

(a) The first consists not of market prices but of average bid and asked prices of the Turman stock for a period of nine months in 1929. As my colleagues note, most courts spurn such a criterion because of its extremely shaky character. Here it is singularly shaky: Only a small part of these shares were on the market. Public information about Turman's affairs was scanty.[37] Turman was owned

37 Moody's Investors Manual, on which my colleagues otherwise rely, in its 1929 edition, after stating that Turman was owned by Eureka, a

BLEED THROUGH POOR COPY

by a company in receivership; and Glass. on October 31, 1929, himself stated, "There is no doubt in my mind that any company can operate out of receivership far more economically than in receivership." Even actual market prices would not reflect the value of the controlling block—82%—of the Turman shares owned by Eureka. Glass, as receiver, in April 1927, purchased, at a private sale, some Turman shares at $9.72 a share, reporting to the court that, if there were an attempt to purchase "any substantial block in the market," the "price would rise substantially" above that figure.

(b) *Capitalization of earnings*:

One of the tests applied by Judge Smith, and the one on which my colleagues primarily rely, is the capitalization of "reasonably to be expected" net annual earnings, ascertained by using actual part average annual earnings. This I think the correct yardstick.[38]

---

subsidiary of MSO, and that MSO was in a receivership, reported merely the following information concerning Turman:

"TURMAN OIL COMPANY: Incorporated in Delaware County 1917, to produce crude oil and natural gas. Company owns leases on 8,423 acres of which about 35% are producing in Mid-Continent oil fields, in Oklahoma and Kansas. Number of wells, 188. Production of oil in April 1927, 10,126 bbls. daily. Capital stock: Authorized $6,000,000; outstanding, $4,629,284; par $10 (changed from $1.00 May 25, 1923). Middle States Oil Corporation owns 82% of outstanding stock. Dividends paid at rate of 1% monthly from October 1921, to June 20, 1923, incl.; also 2% extra each July 20 and October 20, 1922; and 1% extra May 20, 1923. Dividend period changed to quarterly basis in April 1923, July 20, 1923, first quarterly dividend of 3% was paid; none thereafter to April 1, 1929. Daily production, 10,125 bbls. Minority Stockholders' Protective Committee: C. A. Holden, Tulsa, Okla., and J. S. Sheppard, New York, General Counsel."

Moody's 1930 edition contains no data re Turman.

38 See, e.g., *Galveston, H. & S. A. Ry. Co.* v. *Texas*, 210 U. S. 217, 226; *Rock Products Co.* v. *Du Bois*, 312 U. S. 510, 525-526; *Dudley* v. *Mealey*, 147 F. (2d) 268, 270 (C. A. 2).

Judge Smith took the average earnings of Turman for the five years, 1924-1929; allotted 82% to Eureka; capitalized at 10%; and so reached a figure of $1,504,936.78.

My colleagues, after some discussion, conclude that the proper years are not 1924-1929, but the four years, 1925-1929. They also admit (somewhat grudgingly) that, to those earnings, there should be added certain deducted non-recurrent expenses. I agree. My colleagues say, correctly, that thus computed, the average net earnings of Turman for the four years, 1926-1929, were $414,500, and of Eureka, 82% thereof—which is approximately $339,800. Using Judge Smith's capitalization percentage—10%—Eureka's fair market value was $3,398,000.

But my colleagues reject Judge Smith's finding that 10% was the correct capitalization percentage. Instead, my colleagues use 19.31%, and so reach a figure of $1,775,000. In justifying the use of 19.31%, my colleagues rely entirely on an exhibit showing the prices and earnings per share of nine other oil-producing companies in 1929, as reported in Moody's Manual of Investments (1930 ed.).[39] Other than the testimony of Glass, there was no evidence

---

39 This exhibit reads as follows:

EARNINGS PER SHARE OF CRUDE OIL PRODUCERS, 1929

Source: Moody's Manual of Investments, Industrial Securities, 1930 Edition.

Company	*Earnings Per Share, 1929*	*Price 1929*	*Earnings to Price*
Barnsdall Corp.	3.19	20	15.95
Darby Petroleum Corp.	1.13	6½	17.38
Houston Oil Co. of Texas	4.78	26	18.38
Independent Oil & Gas Co.	4.26	17¾	24.00
Lion Oil Refining Co.	4.39	18	24.38
Pacific Western Oil Corp.	1.82	12⅛	15.00
Simms Petroleum Co.	2.79	15	18.60
Skelly Oil Co.	5.28	28	18.86
Superior Oil Corp.	1.06	5¼	20.19
Average for Group—9 Companies			19.31

BLEED THROUGH POOR COPY

whatever that these companies were comparable with Turman. For all we know, they were not, for any one or more of a dozen reasons. Glass briefly testified[40] that they were a "selected" group of companies "that were generally comparable to Turman." He added not a syllable to explain why these companies were "comparable." Most significantly, Judge Smith, who saw and heard Glass when he testified, did not, in his findings, mention that testimony or that exhibit, or even intimate that, from the evidence, any capitalization figure other than 10% was correct. Accordingly, I think that this court—which, of course, did not observe Glass when he so testified—may not properly rely on that evidence, but must accept, as not "clearly erroneous," Judge Smith's finding that 10% is the proper figure.

On April 28, 1941, Glass wrote a letter to stockholders of MSP, concerning the correct valuation of its assets. He supported a valuation based upon a capitalization of four years' average annual earnings (derived from oil operations) at 10.66%, saying, "I would have no difficulty in interesting very shrewd businessmen, clients of mine, amply responsible, in buying the assets of MSP on the basis of that kind of valuation. * * * I would not have the slightest hesitancy in recommending such a purchase and in personally participating with them in such a purchase."

I repeat that, on a 10% capitalization basis, found by Judge Smith to be correct as of December 1929, the fair market value of Eureka was about $3,398,000. Even assuming—an erroneous assumption—that it was proper to take but ⅔ of that value, or $2,265,000, as the fair price at the judicial sale, the actual price paid ($1,450,000) was insufficient in the amount of $815,000.

---

40 He testified, not that he or the reorganization committee had used these figures in 1929, but that he had used them, in preparing to testify before Judge Smith, in order to "check retrospectively."

Even the four-year average may be unfair to the UOP bondholders. For Turman had not had a large production until July 1926. In the short period of some three months, December 31, 1926 to April 10, 1927, its production apparently increased by some 2500%. It may well be, therefore, that the average earnings should be those for the three years, 1927-1929. On that basis, Eureka's average annual earnings were $401,800, which, capitalized at 10%, yields $4,018,000. Even assuming that ⅔ of that sum represented a fair price at the judicial sale, we get a figure of $3,678,000—or $1,228,000 ~~less~~ more than the actual price paid for the Eureka stock at that sale.[41]

---

41 If the average earnings for the five years 1925-1929 are used, then the deficiency on this basis is $594,000, computed as follows:

(a) $374,000 (average annual income) at 10	$3,740,000
(b) 82% (stock of Turman owned by Eureka)	3,066,000
(c) ⅔	2,044,000
(d) Actual price paid	1,450,000
(e) Deficiency	$ 594,000

If the average earnings for the years 1926-1929 are used, but capitalized at 10 (as per Judge Smith), then the deficiency is $815,000, computed as follows:

(a) $414,500 (average annual income) at 10	$4,145,000
(b) 82%	3,398,000
(c) ⅔	2,265,000
(d) Actual price paid	1,450,000
(e) Deficiency	$ 815,000

If the average Turman earnings are taken for the years 1927-1929, the result is as follows:

(a) $490,000 (average annual income) at 10	$4,900,000
(b) 82%	4,018,000
(c) ⅔	3,678,000
(d) Actual price paid	1,450,000
(e) Deficiency	$1,228,000

The valuation reached through capitalization of earnings seems to ignore the fact that Turman, at the time of the sale, had very valuable oil properties which had not yet been brought into production and which therefore did not contribute, in the selected years, to its earnings. The value of those properties should probably be added to the capitalized earnings.

BLEED THROUGH POOR COPY

Be that as it may, it is clear, I think, that, even on the assumption that appellants had the burden of proof, they have shown a substantial loss (aside from any loss on the sale of the unpledged UOP assets, which I shall discuss later). *A fortiori,* is this true, if Glass had the burden of proof.

11. *Judge Smith found that Glass underwrote the fairness of the prices.*

It was Glass' duty, as receiver, to do everything possible to procure the highest prices at the sales. But he did next to nothing in attempting to stir up interest in possible purchasers, in particular purchasers for the Eureka stock. Judge Smith so found.[42]

My colleagues say that on September 25, 1928, on June 1, 1929 and on November 13, 1929, "Glass did establish contact with corporations, American or Canadian, which might have been interested in merging with MSO." But Glass' testimony discloses that, in each of those instances, Glass did not solicit the company: The company sought him. And the meager testimony on this score is that Glass merely supplied such companies with information, did not try to persuade them to buy, and made no attempt to interest them in a purchase of Eureka separately, as distinguished from a purchase of MSO's entire assets. Little weight should be given to this evidence, since Judge Smith, of course aware of it, found that Glass used no real efforts to interest "outside bidders."

Glass had made himself peculiarly responsible for diligence in finding such bidders: In receivers' reports, filed with the court, he had repeatedly proclaimed a "position of disinterestedness" in support of a reorganization which

42 He found: "Glass had an affirmative duty of encouraging bidders. * * * It appears that no intensive efforts were made by the receivers to find outside bidders."

would "accomplish substantial justice to all of the interested parties." In a letter, dated July 29, 1929, incorporated with his approval in the published reorganization plan, he quoted that statement from those reports, said that the published plan did accord "substantial justice to all of the interests involved," and ended by stating that he saw "no reason for the continuance of the receivership and every reason for the prompt consummation of the reorganization, which we strongly urge." In effect, he thus virtually underwrote the fairness of the amount to be paid non-assenting UOP holders, and consequently had an emphatic obligation to stir up potential bidders at the sales. So we said in our previous opinion (154 F. (2d) at 993). Judge Smith so found, stating, "Glass must be held to have underwritten the fairness of the bids." Judge Smith further found that "the repeated representations by the receivers as to fairness of the plan and consideration for the rights of minorities, placed an extraordinary burden upon the receivers * * * to see that substantial, and not only technical, protection was given the minorities no matter how small that proportional interest in any given situation may be." Judge Smith also spoke of the "failure of the receivers more actively to seek and inform purchasers * * * in view of the receivers' assurances to the minority interests," and said that these assurances "made the receivers * * * insurers of the fairness of the plan as well as of the adequacy of the bids." The non-deposited bondholders therefore had a right to believe that the UOP assets could not be sold for a sum sufficient to yield them more than $698 per $1000 bond (face amount).

Judge Smith, despite this finding, quoted above, held Glass not liable, because he found that the price paid for the Eureka stock was fair, a finding which (for reasons above stated) I think "clearly erroneous," especially if Glass had the burden of proof.

BLEED THROUGH POOR COPY

re Eureka

12. *No information to potential "outside" bidders.*

Glass' failure to stir up potential buyers becomes of major importance because the notice of the foreclosure sale of the Eureka stock did nothing to enlighten buyers concerning the assets or earnings of Eureka. That notice—the only one advising that that stock was to be sold—said merely that the sale was being made pursuant to a decree of November 15, 1929, in the suit of Chatham Phenix Bank against UOP, and stated the date, place, and briefly, the terms of the sale. The notice ended with this sentence: "For further particulars, including a more particular description of the terms of sale, intending purchasers are hereby referred to said decree."

The decree was entered in a foreclosure suit which rested on diversity of citizenship, *i.e.*, that suit was not ancillary to the receivership. If a prospective purchaser had read the decree, he would not have seen a word to the effect that Eureka owned some 82% of Turman's stock or referring to the earnings or assets of Turman. The decree did not refer to the receivership or the receivers; and the notice of sale did not suggest any source from which a prospective buyer could learn anything about the earnings or assets of Eureka or Turman.

In this respect, the decree and notice of sale differ, strikingly, from the decree of November 22, 1929, dealing with the sale of the unpledged UOP assets, and the notice of that sale. Nor would anyone reading the notice of sale of the unpledged assets see any reference to the sale of the Eureka stock.

Moreover, one reading the notice of sale of the Eureka stock, had he searched the court records, would not have discovered the data as to Turman's earnings or assets—all of which data Glass had, long before, furnished to the reorganization committee. Glass, Judge Smith and my col-

leagues answer that the reorganization plan, published months before the notice of sale of the Eureka stock, contained this information. But—apart from the fact that the plan omitted the most important part of such information—that plan was not furnished or called to the attention of potential bidders.

If, nevertheless, a prospective bidder for the Eureka shares by some chance had looked at the court's files in the MSO receivership suit, he would not have found the necessary information as to Eureka's and Turman's financial condition, assets and earnings.

But these data were in Glass' hands and were furnished by him to the reorganization committee. In their brief on this appeal, Glass' counsel say: "On April 23, 1928, the inventory of all the physical properties were completed" but "Mr. Glass did not place these seven enormous volumes * * * into the court files." They also say: "Valuation data were freely made available to the reorganization committee and its counsel by Mr. Glass."

As to Glass' argument that, in 1929, it was not the practice to put such data in the court's files: (1) It is discussed *infra* (in point 13 of this opinion); (2) that argument is irrelevant in connection with the lack of information accorded to a prospective bidder for the Eureka stock.

My colleagues say that a prospective bidder "obviously * * * would be someone already acquainted with the Seminole field," and that such a person or groups of persons would surely have kept a watch and been eager to snap up the Eureka shares, so that no loss could have resulted either from Glass' failure diligently to seek or stir up bidders for those shares or from the lack of adequate information in the court files.

That suggestion is most dubious. It is a matter of general knowledge that oil properties in the 1920's were bought by persons or groups—bankers or wealthy persons in other

BLEED THROUGH POOR COPY

businesses—not themselves acquainted with such properties, and that, if they heard of a good "buy," they consulted oil experts.[43] Such persons, if sufficiently informed, might well have bid for the Eureka shares.

Moreover, if I am correct in concluding that Glass had the burden of proof, then it will not do to say, as my colleagues do, that we must assume (absent proof to the contrary) that no informed outsiders would possibly have become bidders, competing with the reorganization committee.

13. *Judge Smith found, correctly, that the judicial sale of the UOP unpledged assets was chilled.*

UOP had unpledged assets consisting chiefly of a claim against MSO. As UOP had almost no creditors other than the UOP bonds, those bonds, for their large deficiency (for principal and unpaid interest, remaining after the receipt of the proceeds of the sale of the Eureka stock) were entitled to almost all the proceeds of the sale of those unpledged assets.

The court, by its decree of November 22, 1929, ordered the sale of those unpledged assets on December 16, 1929. Article Sixth of that particular decree provided: "The receivers shall, not less than ten days prior to the date fixed for sale under this decree, file with the Clerk of the Court a statement "showing and describing as definitely as practicable[44] and made up to the latest day reasonably practicable, but in general terms:

"(1) All of the assets of each of the Holding Companies,[45] and all of the assets which shall have been acquired

---

43 And such was my own experience, in the 1920's, as lawyer for oil companies, investment bankers and other businessmen.

44 Emphasis added.

45 That is, MSO, UOP, Imperial Oil Corporation and Oil Lease Development Company.

by the Holding Companies Receivers in the operation of its business and shall then be held by them; (2) All existing liens and charges created by pledge or deposit of assets of the Holding Companies or any of them as security, specifying the assets which are subject to such liens or charges, the Holding Companies, owning such assets and the amounts of such indebtedness, respectively; (3) All claims for federal and states taxes, interest and penalties then unpaid by or pending against the Holding Companies, respectively; (4) The amount of all indebtedness and liabilities of the Holding Companies Receivers, respectively, remaining unpaid; and all executory contracts which shall have been entered into, assumed or adopted by the Holding Companies Receivers in the operation of the business of the Holding Companies, respectively, or in the performance of their duties as such receivers; (5) All executory contracts to which the Holding Companies or any of them may be parties."

The receivers did, on December 6, 1929, file statements, with the Clerk, each of which was captioned, "Statement Filed by Joseph P. Tumulty and Joseph Glass, Receivers, pursuant to Article Sixth of Decree * * * dated November 22, 1929." [46] Did those statements comply with that direction, *i.e.*, did they describe "as definitely as practicable," but "in general terms," the assets and liabilities? Judge Smith explicitly found that they did not, that those statements—intended to give adequate information to prospective bidders—were decidedly uninformative, "inadequate to enable a prospective bidder to formulate an intelligent

46 Note, once more, that this decree did not cover the sale of Eureka stock, that this decree dealt with the unpledged assets of the several companies, including UOP, that the notice of the sale of these assets did not mention Eureka or Turman, and that, accordingly, one who read the notice of sale of the Eureka stock (under the earlier decree of November 15, 1929) would not learn of the statements filed under the decree of November 22, 1929.

BLEED THROUGH POOR COPY

bid." Indeed, he goes so far as to find that they were "misleading" and that, "certainly the tendency of the" statements "would be to chill the sale."

My colleagues stress the fact that, at the end of each filed statement was a sentence reading, "Further information with respect to the foregoing may be obtained upon request at the offices of the receivers." My colleagues go on to comment on the inadequacy of those filed statements, saying that it is "inconceivable" that anyone seriously interested in the property, upon reading that sentence, would not have made further inquiry of the receivers. But would such an interested person have thought it possible that, if he had inquired of the receivers, he would learn of facts flatly contradicting what the public filed statements declared, *e.g.*, that he would find that, instead of an "undetermined tax liability" (as described in the receivers' statement), that liability not only had been reduced but would be wiped out, and that substantial refunds would be made (a fact known by Glass before the statements were filed)? Would he have thought that the most vital information would be omitted from the statements filed, and that he must procure that information by going to the offices of the receiver within the few—ten—days elapsing between the filing of the statement (December 6) and the sale (December 16)? The very shortness of time made it imperative that the publicly filed statements should contain all the vital data.

In our former opinion (154 F. (2d) at 995), we said that a prospective bidder would naturally assume that the major facts were disclosed in the statements filed, and that any additional information—obtainable by "request" made to the receivers—would be "relatively unimportant, marginal." I see no reason for abandoning what we then said. It is noteworthy that (as Judge Smith said) full disclosure of all these data had been made to the several committees, in-

cluding the reorganization committee, many months before the latter committee arrived at the prices to be paid at the sale. Why should it have been made more difficult for a prospective competitive bidder to obtain these data? The answer, I think, is that Glass had a self-interest to serve in chilling the bidding. Again, it is important that this self-interest imposed on him the burden of proof.

It was a major defect in the filed statements that they left in utter obscurity the amount owing from MSO to UOP. No purchaser, even within the ten days, could have ascertained that amount by asking the receivers. For it was not until December 14, 1929—or two days before the sale—that, by an order of that date, the court even tentatively determined that amount.

My colleagues disagree with Judge Smith who said that, even if potential buyers went to the receivers' office, "No intelligent bid could * * * be made" from the data there available. "Without the benefit of advice on expected recoveries, available to the committees by constant consultation with Glass and his accountant Lind, for any outsiders to bid would have been impossible." Judge Smith also found: "No matter how much time was afforded, it was practically impossible for a bidder to evaluate the intercorporate claims which constituted a fairly large part of the assets without intimate knowledge of their history dug up by the receivers and their accountants in the five years before the sales."

Judge Smith's statement was unquestionably right: The receivers, in their petition of December 14, 1929, which led to the court's order of December 16, 1929, referred to nine volumes of supporting data, showing the details of these accounts, based on reports of experts for which the receivers had paid thousands of dollars. These reports, made in July 1928, and the nine volumes, the receivers had shown,

BLEED THROUGH POOR COPY

long before December 14, 1929, to the committees. The receivers, however, never filed any of these data as part of the public court records, but removed them to the receivers' offices. Glass protests that they were "filed." But the "filing" of a paper means that "it shall remain with the Clerk to be inspected by those who have an interest in it"; the word "filing" carries "with it the idea of a permanent preservation of the thing so delivered and received that it may become a part of the public record." [47] Glass argues that, in 1929, it was not the practice to make such data part of the public court record in receivership cases. But in 1917, James Byrne, a leader of the "reorganization bar," writing of receiverships, said: "It is of the highest importance that at the very earliest moment there should be in the files of the court, for its guidance and that of all parties in interest, as full and clear a report of what the Court has in its hands for administration" as the receivers can prepare. "The report should tell what the assets and liabilities of the company are. * * * " The court sometimes authorizes the receivers to hire experts to aid them in the preparation of such reports." [48] So the court did here, but the receivers did not put the reports in "the files of the court."

The receivers' December 9, 1929 petition, stated: "Your petitioners believe that there will be no opposition to" the proposed order "on the part of any of the parties interested, in view of the fact that the only imaginable source of information in opposition to any of these claims would be the very records from which this data (*sic*) has been de-

47 Judge Lindley, in *Oil Well Supply Company*, 52 F. Supp. 921, 922, citing many authorities.

48 Byrne, Foreclosure of Railroad Mortgages, in Some Legal Phases of Corporate Financing, Reorganization and Regulation, Vol. I (1916) 77, 97.

In the same volume, pp. 153 ff., Paul D. Cravath, writing of reorganization of all sorts of corporations, including industries, referred to the remarks in Byrne's article as applicable generally.

rived." Here the receivers recognized how unenlightening the petition and the December 16, 1929 order were, in the absence of the data they did not put of record. Indeed, the receivers, in their report made in 1928, had said that such data were essential to an informed judgment.

The only "parties interested" to whom the receivers gave notice of the December 16, 1929 petition, were those who had entered formal appearances in the receivership proceedings and the several committees. No notice was published.

The petition prayed, and the order provided, that the intercorporate claims as tentatively adjusted should be "subject to readjustment by further order of the court from time to time upon further showing" of the receivers "but not otherwise." In fact, on May 8, 1930, after confirmation of the sales, the court, on the receivers' petition, further tentatively readjusted the claims in an order again providing for "further readjustment by further order, from time to time upon further showing of the receivers, but not otherwise."

My colleagues concede that this method of handling the intercorporate claims was most unsatisfactory. But they say that this method was necessitated by the court's demand for a speedy reorganization. (Judge Smith and my colleagues suggest that a prompt reorganization was essential because the receivership expenses, if continued, would consume the assets. This, however, seems highly doubtful with respect to Eureka; and it emphasizes the desirability of a separate reorganization of UOP.) However, there is much evidence to indicate that the judicial pressure derived from Glass' belief, and consequent advice to the court, that such speed was desirable: On October 27, 1927, many months before the court began to exert any pressure, Glass had written a letter deploring delay in reorganization because of the receivership expenses, and saying he

BLEED THROUGH POOR COPY

wanted "to be relieved of the burdens of the receivership at the earliest possible moment." Some four months before the decrees of sale, Glass, in his letter of July 29, 1929, incorporated in the published reorganization plan, said he saw "every reason for the prompt consummation of reorganization." The court's pressure was not at all unwelcome to Glass. He never urged that it was undesirable. He thoroughly approved it. In a letter dated October 31, 1929, answering a securityholder who inquired about the reorganization, he said he felt it to the "best interests" of everyone "to have the receivership lifted at the earliest possible moment," that the "receivership can be lifted in about sixty days if the Plan goes through," that the receivers were "anxious to get through" with the receivership, and believed that "the sooner the matter is cleaned up the better it will be for all parties concerned." These were not the sentiments of a man who recognized that haste would lead to the unsatisfactory disposition of important matters and who reluctantly submitted to the court's request for haste. The sloppy job with reference to the intercorporate claims cannot, then, be ascribed to the court's demands.

Nor can judicial pressure—which, according to Glass, commenced early in 1929—explain why the so-called adjustment was made only two days before the sale: In their third report, filed on May 27, 1928, the receivers had said that "balance sheets for all companies are now in process of completion, which balance-sheets will show in detail the intercompany claim situation"; that engineers were at work "completing their appraisals";[49] that "the valuations thus arrived at will be used as the basis for proper book entries as of January 1, 1928"; that "balance sheets have been tentatively prepared with blanks left for the insertion of these figures derived from those valuations," and "in

49 The valuations were received in July, 1928.

these balance-sheets tentative treatment will be given to intercorporate accounts." The receivers added: "It is the purpose of the receivers thereafter to present recommendations to the court for the disposition, without litigation, of these intercorporate accounts upon notice to all interested parties. * * * Fortunately, the end is in sight. The complications which remain are few in number." This was about one and a half years before the receivers filed their petition on which the court based its order of December 14, 1929.

And why, at the very latest, could not the tentative "adjustment" have been made soon after the plan's publication on July 29, 1929?

The time-table of events is revelatory:

Receivers' Third Report	May 27, 1928
Reorganization plan published	July 29, 1929
Decree of sale of unpledged assets	Nov. 22, 1929
Notice of this sale	Nov. 26, 1929
Receivers' Statements filed with the Clerk	Dec. 6, 1929
Order tentatively adjusting intercorporate claims	Dec. 14, 1929
Sale of Unpledged Assets	Dec. 16, 1929
Confirmation Order	Dec. 24, 1929

But even if we ascribe the unsatisfactory and tardy method of tentatively adjusting these claims to judicial pressure for speed, it is difficult to comprehend why the UOP claims against MSO which (as my colleagues say) had been "liquidated," by the order of December 14, 1929, at $1,370,000, should have been valued by the reorganization committee and Glass at some $300,000, and why they fixed its sale price at some $200,000. My colleagues say of these

BLEED THROUGH POOR COPY

low figures, "We do not know how they were reached, nor is it necessary that we should; they stand unless they are shown to be incorrect and they have not been." If, however, Glass had the burden of proof, then it was necessary for him to show how these figures were reached and that they were correct and fair.

If UOP had been separately reorganized, its claim against MSO would not have been sold but enforced.

I recur to the fact that no one has explained why UOP was not separately reorganized. Had it been, the new (reorganized) UOP would have been in a position to assert against MSO its creditor claim which (according to the receivers) amounted to at least $1,730,000. In such circumstances, that claim would not have been sold at a judicial sale but would have been litigated or settled—and not on the basis of a mere guess that it was worth only $300,000.

Because of Glass' non-disclosure of his personal interests, he may be required to repay part of the compensation paid him as receiver of UOP.

Since Glass did not, before confirmation of the sales, disclose to the judge his personal interests, and because the judge acted on Glass' tainted advice, Glass may be required to repay part of the compensation paid him as receiver.[50]

---

50 See, e.g., *Crites, Inc.* v. *Prudential Company*, 322 U. S. 408, 418; *Woods* v. *City Bank*, 312 U. S. 262, 268; *Wadsworth* v. *Adams*, 138 U. S. 380, 388; Mechem, Agency (2d ed. 1914) Sec. 1588; Restatement of Agency, Sec. 390 and Comment f, Sec. 469 and Comment c; *Warren* v. *Burt*, 58 Fed. 101, 103 (C. A. 8); *Beatty* v. *Guggenheim Exploration Company*, 223 N. Y. 294, 304; *Everhart* v. *Searle*, 71 Pa. St. 256; *Little* v. *Phipps*, 208 Mass. 331, 333-334; *Rice* v. *Wood*, 113 Mass. 133; *Lemon* v. *Little*, 21 So. Dak. 628, 636-637; *Tracy* v. *Willys Corp.*, 45 F. (2d) 485 (C. A. 6).

14. *Boyd-case rule violation*

My discussion thus far has dealt with those aspects of the case unrelated to the doctrine of *Northern Pacific* v. *Boyd*, 228 U. S. 482. I now turn to that doctrine. I think that it was violated here, and that therefore Glass is liable because he aided that violation and, in so doing, was guilty of disloyalty to the UOP bondholders, since he was serving his personal interests.

In our former opinion, 154 F. (2d) at 999, we said: "The Boyd case principle was violated if stockholders or creditors of Middle States, without adequate consideration, received under the plan a participation in United assets and if United bondholders were not offered in the plan the equivalent of payment in full, since even the creditors of Middle States were not creditors of United but creditors of a stockholder of United." Significant here is the fact that (as previously observed) contrary to then well-established practice, the reorganization committee did not submit the plan to the court, and the court, before confirming the sales, refrained from holding, pursuant to notice, a hearing on, and passing on, the fairness of the plan.

Unquestionably (as shown *infra*) the plan, in several important respects, disturbed the position of the UOP bonds with reference to Eureka and the unpledged UOP assets, and allowed MSO stockholders and its creditors to participate in the new company, in such a manner that they were benefited by the new company's ownership of these UOP assets.[51] Glass testified that in November 1929 "there was no equity in the MSO Corporation—no residuum of equity available for stockholders." Judge Smith found

51 Of the MSO serial notes—given a substantial participation in the new company under the plan—Judge Smith found they "were of doubtful validity, to say the least." The holders of those notes were but creditors of UOP's stockholders, MSO.

BLEED THROUGH POOR COPY

that it was then insolvent and that "the old MSO stockholders as such did not provide any new consideration."

Judge Smith said that the fact that assets were provided by others did not make the *Boyd* rule inapplicable so far as the MSO stockholders were concerned. I shall, however, assume, *arguendo*, that this conclusion would not necessarily be correct, if (1) a "system" reorganization were essential, and (2) the contributed assets had a worth sufficient to give the UOP bondholders the equivalent of their displaced rights.

However, the "equivalent" doctrine—permitting stockholders to participate, despite displacement of senior creditor rights, if the reorganization plan provides an equivalent for those displaced rights—does not apply unless the participation of stockholders in the reorganization is essential. See, e.g., *Kansas City Terminal Company* v. *Central Union Trust Co.*, 271 U. S. 445: "Generally, additional funds will be *essential* to the success of the undertaking, and it may be impossible to obtain them, unless stockholders are permitted to contribute and retain an interest sufficiently valuable to move them. In such or similar cases, the Chancellor may exercise an informed discretion concerning the practical adjustment of the several rights."[53] In *Consolidated Rock Products Company* v. *Du Bois*, 312 U. S. 510, 529, the court held that the "absolute priority" rule precludes participation by stockholders unless there is "a necessity of seeking new money from them" (or new assets). But here (as I think I have shown above) so far

---

52 See *Railroad Company* v. *Howard*, 7 Wall. 392, and the discussion of that case, as affecting the *Boyd* doctrine, in Frank, Some Realistic Reflections on Some Aspects of Corporate Reorganizations, 19 Va. L. Rev. (1933) 542, 544-547.

53 Emphasis added.

Cf. *Kansas City Railway* v. *Guardian Trust Company*, 240 U. S. 166, 178.

as UOP was concerned, a "system" or "merger" reorganization was not essential, *i.e.*, UOP could easily have been separately reorganized and such a separate reorganization would have been better for the UOP bonds. Therefore, displacement of their rights was not justified: Surely, when insolvent Company A could be reorganized by itself, and so reorganized, could easily obtain all needed additional funds, it is not lawful to merge it with insolvent Company B under a reorganization plan which cuts off some of the substantial "absolute priority" rights of Company A's creditors, and gives those rights to its stockholders, merely because Company A's creditors receive an equivalent of their reduced rights in the form of securities of the new company resulting from the merger. (It does not concern us here whether a different rule would govern were one of the companies a railroad or public utility; see *First National Bank* v. *Flershem*, 290 U. S. 510.)

However, in the balance of this *Boyd*-rule discussion, I shall generally assume, *arguendo*, that a "system" reorganization was essential. On that assumption, in order to make the plan fair to the UOP bondholders, it was necessary that the new company have assets, theretofore not available to the UOP bonds, of sufficient value to make up for the rights of which the UOP bonds were deprived.

The plan did displace the rights of the UOP bonds as follows:

(1) The new bonds allotted to them bore interest at 6½%. The old bonds carried interest at 8% plus "interest participation" not exceeding 20¼%. The new bonds were thus "an inferior grade of securities." [54]

---

54 *Consolidated Rock Products Company* v. *Du Bois*, 312 U. S. 510, 527-528.

See also Judge Learned Hand in *Eddy* v. *Prudence Bonds Corporation*, 165 F. (2d) 157, 160-161 (C. A. 2).

BLEED THROUGH POOR COPY

(2) The old bonds matured by their terms on July 25, 1931. The new bonds matured on January 1, 1945. Again this made the new bonds "inferior." [55]

(3) For the purpose of allotting new securities, the UOP bonds were entitled to their principal plus accrued interest, to the effective date of the plan, or about $4,450,000. Instead, the plan computed interest at but 8% up to July 29, 1929, making a total, for principal and interest, of but (about) $3,350,000.

(4) The UOP bonds, being entitled to virtually all the UOP assets, were in a position, on a reorganization of UOP, to obtain voting control. Under the plan, they received far less than a majority of the new company's Class A stock and none of the Class B stock.[56] But stockholders and other creditors of MSO (stockholders and creditors of the stockholders of UOP) received a majority of the Class A stock and the overwhelming majority of the Class B stock, thus putting ultimate voting control in their hands.[57]

---

55 *Consolidated Rock Products Company* v. *Du Bois*, 312 U. S. 510, 527-528.

56 *Consolidated Rock Products Company* v. *Du Bois*, 312 U. S. 510; *In re Chain Investment Company*, 102 F. (2d) 323, 324-325 (C. A. 7); *Highland Towers Company* v. *Bondholders' Protective Committee*, 115 F. (2d) 591, 600 (C. A. 7).

57 UOP and OLD bondholders were given approximately 58,000 shares of A stock out of 300,000 issued, and no B stock. Serial noteholders received 180,000 shares of A stock, 60% of the issue. 745,000 of the 895,000 shares of B stock issued went to old stockholders, and another 107,000 shares of B stock went to serial noteholders. Together the old stockholders and serial noteholders received almost 95% of the B stock.

The Plan called for depositing all A and B stock in a voting trust, with full voting powers vested in five trustees. The trustees were to be selected by the Reorganization Committee as follows:

2 persons whom the Reorganization Committee (which included repre-

Did the plan contain a "full compensatory provision * * * for the entire bundle of rights" [58] of which the UOP bonds were deprived? It is suggested that this requirement does not apply where, as here, a reorganization involves a "merger." I do not agree.[59] A reorganization which vio-

---

sentatives of junior interests) believed to be impartial as among holders of various classes of securities;

1 person approved by the Bondholders' Committee;

1 person approved by the Serial Noteholders' Committee and Gulf Coast Committee;

1 person approved by the Stockholders' Committee.

During the duration of the voting trust (ten years, subject to earlier termination by action of the trustees) the Board of Directors was to be constituted as follows:

1. During the first year of the trust, the Board was to be selected by the Reorganization Committee and to consist of three persons believed by them to be impartial as among holders of various classes of securities, two persons approved by the Serial Noteholders' Committee, one by the Gulf Coast Committee and two by the Stockholders' Committee.
2. During subsequent years of the trust: 3 directors chosen by the two impartial trustees, two chosen by the trustee approved by the Bondholders' Committee, 2 by the trustee approved by the Serial Noteholders' and Gulf Coast Committees and 2 by the trustee approved by the Stockholders' Committee.
3. Upon the retirement of the new bonds the number of directors was to be reduced by 2 and the voting trustee approved by the Bondholders to cease to act.

After termination of the voting trust, A shareholders were, as a class, to elect 4 directors, and B shareholders, as a class, to elect 4 directors. A and B shareholders would also vote, as classes, for a ninth director, but the position was to be vacant unless the same person was voted for by holders of both a majority of A stock and a majority of B stock represented at the election.

Neither A shareholders nor directors elected by them (nor, during the voting trust, trustees approved by Committees representing them) were to be permitted to vote on the question of redeeming A stock or in favor of voluntary dissolution or liquidation of the company.

58 *Consolidated Rock Products Company* v. *Du Bois*, 312 U. S. 510 at 528.

59 That the *Boyd* doctrine applies to a merger, even of railroad companies under Sec. 77 of the Bankruptcy Act, see, e.g., *R. F. C.* v. *Denver & Rio Grande Western R. Co.*, 328 U. S. 495.

BLEED THROUGH POOR COPY

lates the *Boyd* doctrine is a fraudulent conveyance; and clearly a fraudulent conveyance can result from a merger.

My colleagues suggest that this reorganization was so complex that, to determine whether the *Boyd* doctrine was violated, is an horrendous achievement. However, if I am correct in concluding that Glass had the burden of proof, then it was up to him to show that, in displacing the previous rights of the UOP bondholders, enough was supplied by way of substitution for the displacement of the UOP bond rights.

It may well be, as my colleagues say, that, if Glass had had no personal interest in achieving the reorganization then, as he would have been merely a "meddling outsider," the bondholders could assert a claim against him for any conduct which fell foul of the *Boyd* doctrine, only to the extent that they could prove an actual, specific, resultant loss. But, once more, this ruling tumbles if Glass had the burden of proof.

Here again enters the question, discussed above, of the fair going-concern value of Eureka. For that a fair price was paid at the forced sale of Eureka does not answer the *Boyd*-case question: The unfairness of the offer in a plan is not cured simply because the alternative is a proper share of the price paid at such a sale. Both alternatives must be fair.

So, too, as to the fair going-concern value of the unpledged UOP assets. Judge Smith says that, at the forced sale, the UOP claim against MSO was "sold at a fair price," (*i.e.*, $200,000). But again, even were that price fair, that fact would not meet the Boyd problem. The receivers, as we have seen, obtained an order on December 14, 1929, "liquidating" that claim at $1,730,000. True, they "valued" it, before the sale, at $300,000. But, as my colleagues concede, that "valuation" was pure guesswork.

Since Glass had the burden, it was up to him to prove that it was not worth at least $1,730,000.

Judge Smith seeks to get rid of the question of the fair value of that claim by saying that "any claim under the Boyd rule as to that debt is washed out on its acquisition by Middle States Petroleum" (*i.e.*, the new company). Not at all—unless the new securities allotted to the UOP bondholders gave them the equivalent of their rights in the UOP assets.[60]

In this connection, my colleagues once more employ the "judicial pressure" argument to justify the $300,000 valuation fixed by the reorganization committee and Glass. But, assuming, *arguendo*, the cogency of that argument with respect to the fairness of the price paid at the judicial sale, it cannot excuse the use of that figure for purposes of ascertaining the fairness of the plan. Judge Smith, speaking of the plan's provisions as they affected another interest (Southern States), said that "Some plan undoubtedly could have been worked out which would have adjusted the accounts between the corporations" (as of the date of the adoption of the reorganization plan) "and provided additional" securities to be issued later when the accounts were finally adjusted.[61] The same is true as to the UOP claim against MSO: The plan, to be fair, should have provided that securities were being reserved for issu-

---

60 Had UOP been separately reorganized, there would have been no sale of its claim against UOP, which was in amount at least $1,730,000.

The separately reorganized new UOP would have been in a position to demand that, for its claim, it receive new securities under a fair plan just as such securities were allotted to so-called "outside" creditors of MSO for their claims.

61 Judge Smith also said, of certain "minority interests," that whether they "were entitled to priority over the old stockholders, or whether they were entitled only to some sort of distributive share, some provision should have been made more effectively to protect them."

This comment should be applied to the UOP bonds.

BLEED THROUGH POOR COPY

ance to the UOP bonds, if, upon subsequent examination, the value of that claim should turn out to exceed $300,000. Such a provision would, in a simple way, have obviated the unfairness created by the pressure for speed.

Here it should again be noted that, as Judge Smith said, Glass and the reorganizers "probably desired to effect a reorganization to be controlled by the interests represented on the reorganization committee." [62]

Unfairness in cancelling the option to deposit at a time when a non-depositing bondholders could not know the amount of cash distributable to him if he failed to deposit.

Judge Smith found: "The receivers made no affirmative effort to inform non-depositing United bondholders of facts upon which the bondholders could determine for themselves whether acceptance of securities under the plan or cash distributive values would be in the bondholders' best interests." Nor could any such bondholder so determine until he knew the amount of cash he would receive if he failed to deposit under the plan. And this he could not know until the court fixed it at about $698 per $1000 bond (face amount). Meanwhile, on May 14, 1930, the right to deposit was cut off. In these unusual circumstances, that cut-off was most unfair. The situation was unusual—and thus unlike *Jameson* v. *Guaranty Trust Company,* 20 F. (2d) 808, 815 (C. A. 7), cited by Judge Smith and my colleagues—because, in the usual case, the securityholders know, before the cut-off, exactly the amount of cash they will receive if they elect not to deposit.

---

62 Of course, if the fair going value of (1) Eureka plus (2) the unpledged UOP assets, exceeded the $4,450,000 (approximately) owing to the UOP bondholders, it was not improper to allot, under the plan, the excess to junior interests—provided a "system" reorganization was essential.

Here the non-depositors had no such knowledge until July 25, 1933, when their distributive share of cash was fixed at about $698 per each $1000 bond (face amount). That distributive share bore no interest from the date of the sales' confirmation to July 25, 1933. On September 12, 1930, Glass, as president of the new company, reported that it had made "a very considerable saving" as a result of the cut-off. He was then still a receiver of UOP.

Accordingly, all else aside, the plan was unfair because there was not in it a "tender made and kept good" [63] of new securities to the UOP bondholders. (It is interesting that the Class B shares, allotted to the old MSO stockholders, apparently had a market value of some $10,000,000 in September 1952.) I think that Glass, who served his own personal interests in helping to consummate the plan, is liable for any resulting loss to UOP bondholders who did not deposit during the period from the end of 1929 to July 25, 1933. "What constitutes a fair opportunity of participation may depend on the circumstances. A fair time limit may be set, but otherwise a bondholder cannot be excluded unless he is informed of all relevant facts." [64]

I cannot agree with my colleagues that those bondholders have no cause for complaint because they did not ask for an extension of the offer beyond May 14, 1930: It was not up to them to see that the plan made them a fair offer.

My colleagues say that bondholders who "were delaying their choice until the distribution dividend was fixed, should have communicated with the committee or the receivers," and therefore "are in no position to complain" if they were cut off without so communicating. The short

---

63 See *Northern Pacific Ry. Co.* v. *Boyd*, 228 U. S. 482 at 508.

64 Rodgers, Rights and Duties of the Committees in Bondholders' Reorganizations, 42 Harv. L. Rev. (1929) 899, 903 note 13, discussing *Jameson* v. *Guaranty Trust Company*, 20 F. (2d) 808 (C. A. 7).

BLEED THROUGH POOR COPY

answer is that the committee and the receivers could not have told anyone, in May 1930, what the "distribution dividend" would be in July 1933.

My colleagues also say: "Judge Knox had decided that the receivership, already six years old, must be ended; and if MSP (the new company) was to have a start unhampered by the past, it was essential that it should know how many of the old bonds would be refunded and how many it must pay off in cash. That could not be known until the options had expired; and not until then could Judge Knox' decision be put into effect." This assertion rests on a fallacy: Judge Knox merely directed that the assets be taken out of the receivership. He did not concern himself with the adventures of the new company, once the sales to it (via the reorganization committee) had been confirmed. In fact, he held that, after confirmation, he had no jurisdiction re the new company's affairs. And, note again, he did not, after notice and hearing, determine the fairness of the offers in the plan to non-depositors.

Glass, at the time of the cut-off, was still UOP receiver and was also the new company's president. Before becoming president of the new company, he had (so Judge Smith found) "an understanding with the company that, in any case in which the company's interest conflicted with his position as receiver, he would act as receiver and not for the company." Here he signally failed: As UOP receiver, he assured non-depositors of the plan's fairness. He therefore had the duty to see that the plan's offer was fair, *i.e.*, kept open until a non-depositing bondholder could know the alternative to accepting the offer. But, as already noted, Glass, the new company's president, had a conflicting interest to terminate the offer before such knowledge was possible. The cut-off in 1930 favored that conflicting interest.

As reflecting his attitude, it is relevant that, after Glass became president of the new company while still remaining receiver, he favored the interests of that company, or his own direct interests, opposed to those of minorities interested in receiverships other than UOP. Thus Judge Smith found that Glass and his family purchased stock in the new company without disclosing that fact to the court; that, as receiver, he sold securities or claims to the new company, without the court's approval; and that, as receiver, he caused receivership companies to make large loans to the new company, without court orders.

15. *Summary of disadvantages to UOP bondholders of a "system" reorganization.*

If, in place of a "system" reorganization, the UOP bondholders had, through judicial sales of the UOP assets, acquired all those assets, they would not have suffered these serious disadvantages:

(1) There would have been no price for any of those assets tailored to a "system" reorganization.

(2) There would have been no excuse of haste to support a sale of the huge claim of UOP against MSO. By litigation (or settlement of threatened litigation) of that claim, they might well have collected substantially more than the $200,000 for which that claim was sold in circumstances which made an intelligent "outside" bid impossible.

(3) They would have obtained undiluted ownership and management of Eureka and would not have been asked to accept any displacement of their rights and to receive "inferior" securities as the equivalent of such displaced rights, securities whose value it was most difficult to evaluate.

BLEED THROUGH POOR COPY

16. *MSP (the new company) and the fraudulent conveyance.*

In the usual *Boyd* case situation, the attack is on the old stockholders as grantees of a fraudulent conveyance. Where there are innocent investors in the new company, and many of the old stockholders have sold their new securities, the courts usually require the new company to issue, to the non-assenting bondholders, new securities, which will not work harm to the innocent investors. But the old stockholders, nevertheless, are the fraudulent grantees. My colleagues say correctly that the grantee in a fraudulent conveyance is immune, unless the grantor had an actual "intent to defraud," if any fair consideration passed to the grantor.[65] I have much doubt whether here the consideration came within that category.

There still remains the question of the statute of limitations or laches. The "fraudulent conveyances" here were accomplished through sales by a special master appointed by a federal court. It would seem that, as this involved the integrity of the federal judicial process, the New York Statute of Limitations, and the New York laches doctrine, would not apply. My colleagues say, however, that, since appellants did not appeal from the order confirming the sales, no federal question is involved in their collateral attack on the sales as fraudulent conveyances. I have much doubt on that score. For when a fraudulent conveyance, achieved through a judgment, is attacked, after the time for an appeal from the judgment has elapsed, the attack, although collateral, is on the judgment. However, although with grave misgivings, I concur in my colleagues' conclusion that no order against MSP should be entered.

---

65 See, e.g., *Stronin* v. *International Acceptance Bank, Inc.*, 70 F. (2d) 248, 252 (C. A. 2); New York Debtor and Creditor Law, Sec. 274 (being the same as Sec. 5 of the Uniform Fraudulent Conveyance Act).

17. *No laches. Cohen and appellants not chargeable with knowledge privately possessed by the UOP bondholders' committee or the reorganization committee.*

No one suggests that Cohen knew, or reasonably should have known, of Glass' personal interests adverse to those of the UOP bondholders, or had been advised as to the date concerning valuations and other important matters not put of record in the receivership. Judge Smith has found that Cohen was not so informed that appellants are barred by laches. My colleagues do not question that finding; and they agree, with our conclusion in our earlier opinion (154 F. (2d) at 1000-1001), that, if Glass, as federal court receiver, violated his loyalty-duty, no state statute of limitations would bar the claim against him.

Glass still seems to urge, however, that because Cohen deposited some of his UOP bonds under the plan, he and his representatives, *vis à vis* the bonds he did not deposit, must be charged with knowledge of facts he did not know but which were known to the UOP bondholders' committee. We answered such an argument, as follows, in our former opinion (154 F. (2d) 996, 998); "In other words, appellees' position, in effect, seems to be that the receiver discharged their fiduciary duty, owing to all United bondholders, when they made full disclosure to the committee representing those who deposited. Of course that is not true. The receivers represented all non-depositing as well as depositing claimants, but the committee did not. Fully to inform non-depositors was as much the duty of the receivers as to inform the committee. The very fact that no committee represented non-depositing United bondholders imposed on the receivers an obligation to keep them fully informed, to make essential information as easily accessible to them as was practicable. Appellees, however, contend that all information obtained by the committee representing de-

BLEED THROUGH POOR COPY

posited United bonds must be imputed to Cohen. We here assume (without indicating a possible qualification) that Cohen, in his capacity as a holder of deposited United bonds, and with respect to such bonds, must be treated as having had such knowledge 'constructively.' But absent any proof that actually (not merely 'constructively') Cohen had such knowledge, we do not agree that it is to be imputed to him in his capacity as a holder of the non-deposited bonds, or to the person or persons who previously held those bonds. * * * Since appellants seek no relief with respect to the United bonds which Cohen exchanged for new securities under the plan, we need not consider whether that exchange would have barred appellants had they sought, with respect to those bonds, to surcharge the receivers. But we cannot agree that that exchange of those bonds prevents appellants, as successors of Cohen with respect to the unexchanged bonds, from thus seeking to surcharge. As to those bonds, Cohen was in no different position from any other holder of undeposited bonds. There is nothing to show that he had better information than any other such holder; and no such holder, unless (unlike Cohen) he received special advice from the receivers or the committees, was informed of the data in the hands of the receivers. * * * The record does not support the statement of the district judge[66] that Cohen 'had full knowledge of what was done with respect to the assets' of United and 'also had complete appreciation of the significance there,' if the judge meant that Cohen was informed of the values and accounting." [67]

---

66 The reference was to the receivership judge, not to Judge Smith.

67 That "constructive" knowledge is a fiction, and not to be equated with actual knowledge, see *Schoedel* v. *State Bank of Newburg*, 245 Wis. 74, 76; cf. *Mullane* v. *Central Hanover Bank & Trust Co.*, 339 U. S. 306; *City of New York* v. *N. Y., N. H. & H. RR. Co.*, 344 U. S. 293; *McDonald* v. *Mabee*, 243 U. S. 90.

Moreover, even if appellants were barred by laches, Glass should be surcharged for the benefit of all other holders of undeposited UOP bonds. For, as we said in our former opinion (154 F. (2d) at 992, note 13): "The surcharging is not limited to an amount measured by the interest of the particular person thus objecting to the receiver's accounting, since the surcharge is for the benefit of all similarly situated persons. For the court, in administering the estate in its custody for all the beneficiaries, must see to it that none of them suffers because of the misconduct of its receiver, and the discharge of that obligation should not depend upon their appearance in court to voice their objections to that misconduct. Cf. *Moon* v. *Wineman*, 57 Minn. 415, 59 N. W. 494, 495. Thus, if the judge learned of the misconduct from a wholly neutral source (cf. *Investment Registry* v. *Chicago & N. E. Ry. Co.*, 212 F. at p. 608), he should surcharge the receiver and distribute among all interested the money owing to the estate by the receiver because of that misconduct." We also said (154 F. (2d) at 1002): "Appellants have the right, for their own benefit and that of other holders of non-deposited bonds to have Glass surcharged on account of his wrongdoing, if any. In so holding, we do not mean that, even if appellants lacked that right, the district court should have disregarded the merits of appellants' charges against Glass and should have refrained from directing an investigation for the benefit of whatever persons may have been injured by Glass' alleged misconduct."

18. *Glass' major derelictions summarized.*

Here is a summary of Glass' major derelictions:

(1) He urged and helped to consummate a "system" reorganization, to his own benefit, and did not propose a separate UOP reorganization which would

BLEED THROUGH POOR COPY

have been far more beneficial to the UOP bondholders.

(2) He had a personal interest in fees, payments of which depended on the sales in aid of the "system" reorganization, but he did not disclose that interest to the judge until after confirmation of the sales.

(3) He had a personal interest in becoming lawyer for the new company which would result from the "system" reorganization, but he did not disclose that interest to the judge.

(4) By repeated assurances to all securityholders, he virtually underwrote the fairness of the plan and, alternatively, the price paid for the Eureka stock, but he did not discharge his duty of diligently seeking purchasers for that stock.

(5) He agreed to prices tailored to the "system" reorganization.

(6) He deviated from the normal practice of putting in the permanent public court record important data (which he privately made available to the committees).

(7) He acquiesced in the departure from the standard practice of having a court hearing, on notice to all interested persons, concerning the plan's fairness.

(8) As UOP receiver, he owed a duty to keep alive the offer to non-assenting bondholders until they could learn the amount of cash they would receive if they did not deposit; instead, he yielded, as the president of the new company, to the conflicting interest of that company which gained by the cut-off of the offer before the bondholders could learn that amount.

(9) He delayed, without explanation, for many years in filing his final account, with the consequence that witnesses died and documents were lost; in the interval, he resisted efforts of interested persons to obtain vital information about the receivership, which he had not put in the court files.

All this does not add up to "innocence." These derelictions would have been bad enough if Glass had been a layman. They were worse because he was a lawyer, with the obligations which our profession exacts of its members.[68]

In more concrete terms, the salient features of the story are as follows: Glass, originally a lawyer representing stockholders of UOP, becomes its receiver and is handsomely rewarded for that service.[69] Having a continued, personal interest in the welfare of the stockholders, because of unpaid fees owing to him from them, he promotes, and helps to put through, a reorganization. This reorganization favors the stockholders and injures the holders of undeposited UOP bonds. It involves the creation of a new company in which UOP's valuable assets are not only merged but submerged, a company for which, before the judicial sales—essential to that reorganization—he had been virtually assured he would be counsel. As a consequence of that reorganization, he receives fees (as counsel for the stockholders' committee) which could not otherwise have been paid. Before confirmation of the judicial sales, he does not disclose his personal interests to the judge. A few weeks after confirmation of the sales, he becomes president of the new company at a splendid salary.[70] As presi-

68 See, *e.g.*, Drinker, Legal Ethics (1953) 74, 103-106, 109.

69 Meanwhile, he still engages in practice as a lawyer.

70 Glass' annual salary was initially $50,000. During the depression it was reduced to $24,000 but was subsequently increased and is now about $56,000.

BLEED THROUGH POOR COPY

dent, and still UOP receiver, he soon favors the new company where its interests conflict with those of the holders of undeposited UOP bonds. Ever after, he remains UOP receiver and president of that company, and controls it.[71] He and his family buy and now own a highly valuable block of its outstanding securities.[72] All this he achieves by means which caused a serious loss to bondholders for whom he was obligated to act as a fiduciary. I think a federal receiver may not thus misuse his position.

---

71 Judge Smith found that Glass and a group friendly to him have "control and management" of the new company, and "that he has greatly profited over the years from his association" with it. He also found, "The boards of directors of the new corporation have been friendly to Glass' management and have contained several members who, by reason of employment by the corporation or by association with Glass in his law firm, have been closely connected with him." And he found that the voting trust, which "ran out after ten years," was renewed, and that Glass, from the beginning, has been a voting trustee. The voting trust no longer exists.

72 Judge Smith found that Glass and his family own 8% of the voting trust certificates for Class A stock, the sole class of securities now outstanding since the bonds of the new company were retired on January 1, 1945.

Large dividends have been paid on that stock, which is now worth several millions of dollars.

BLEED THROUGH POOR COPY

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

[SAME TITLE.]

Before: L. HAND, SWAN and FRANK, Circuit Judges.

On Petition for Rehearing

Meyer Kraushaar for the petitioners.

PER CURIAM: The petition for rehearing and for correction of the opinions, majority and dissenting, filed February 7, 1955, is denied in all respects except as to the question of costs and disbursements on the appeal. The appellees may have until March 9th to file any objection they may wish to make to the denial of costs to all parties, and that each party shall bear its own disbursements, the cost of printing the "Joint Appendix" to be borne, one half by the appellants and the other half by the appellees, in such proportions among themselves as they may agree.

L. HAND
J. N. FRANK
THOMAS W. SWAN

Dated: February 21, 1955

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 284—October Term, 1953.

(Submitted March 15, 1955 Decided March 25, 1955.)

Docket No. 22426

JOSEPH A. PHELAN,

Complainant,

—v.—

MIDDLE STATES OIL CORPORATION, *et al.*,

Defendants.

MEYER KRAUSHAAR and SOPHIE D. COHEN, as sole surviving Executors under the Last Will and Testament of William W. Cohen, deceased, SOPHIE D. COHEN, individually, and LEVY BROS.,

Objectants-Appellants,

—v.—

JOSEPH GLASS and JOSEPH P. TUMULTY, as Receivers of UNITED OIL PRODUCERS CORPORATION and MIDDLE STATES PETROLEUM CORPORATION,

Appellees.

Before:

L. HAND and SWAN,

Circuit Judges.

On the award of Appellate costs.

BLEED THROUGH POOR COPY

PER CURIAM:

On February 21, 1955, in our memorandum denying the appellants' petition for rehearing, we said that the appellees might have until March 9th to file any objections they might have to the denial of costs to all parties and that each party should bear its own disbursements, the cost of printing the "Joint Appendix" to be borne one half by the appellants and the other half by the appellees. The attorney for Middle States Petroleum Corporation—MSP—filed an affidavit, and a reply thereto was filed by the attorney for the appellants. It now appears that Glass did not pay any part of the expense of printing the "Joint Appendix," but that MSP paid the whole amount. Our reason for not taxing the appellees' disbursements was because the court was not unanimous, which showed that the appeal was not unjustified. However, the court was unanimous as to the dismissal of the claim against MSP, because of the bar of the Statute of Limitations; and we can therefore see no reason why the entire cost of printing the "Joint Appendix" should not be borne by the appellants. There can be no question that this expense was necessary to a disposition of the appeal, and we are not disposed to regard the action as one brought in the public interest by Cohen's executors, Levy Brothers and Sophie Cohen, individually; only the U.O.P. bondholders had any interest in the outcome and a very small fraction of them.

The printing cost of the "Joint Appendix" and "Supplemental Record"—$11,710.82—will be assessed against the appellants. Otherwise no costs or disbursements will be awarded to any party.

REPORTED 203 FED. (2) 836

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 128—October Term, 1952.

(Argued March 5, 1953 Decided April 30, 1953.)

Docket No. 22426

JOSEPH A. PHELAN,

Complainant,

—v.—

MIDDLE STATES OIL CORPORATION, *et al.*,

Defendants.

Before:

SWAN, *Chief Judge*, L. HAND and FRANK, *Circuit Judges.*

Appeals from the United States District Court for the Southern District of New York, J. Joseph Smith, *Judge.*

Meyer Kraushaar and Sophie D. Cohen, as sole surviving executors under the Last Will and Testament of William W. Cohen, deceased, Sophie D. Cohen individually and Levy Bros. appeal from certain parts of an order entered in the above entitled equity receivership after a lengthy trial on their objections to the accounting of Joseph P. Tumulty and Joseph Glass as receivers of United Oil Producers Corporation. Middle States Petroleum Corporation

BLEED THROUGH POOR COPY

appeals from so much of said order as dismissed its cross-claim against the executors of William W. Cohen, deceased.

MEYER KRAUSHAAR, *Attorney for objectants-appellants.*

LESLIE KIRSCH, *Attorney for receivers of United Oil Producers Corporation, appellees.*

RALPH MONTGOMERY ARKUSH, *Attorney for Middle States Petroleum Corp., appellee and cross-appellant.*

PER CURIAM:

A prior order which discharged the receivers was reversed by this court in *Phelan* v. *Middle States Oil Corporation*, 154 F. 2d 978. After remand a lengthy trial was had on objections to the receivers' accounting, and the present appeal is from the order entered after such trial. That order contained nine numbered paragraphs which provided in substance as follows:

1. It directed, pursuant to Rule 54(b), that final judgment be entered upon the claims determined in paragraphs 2 through 8 but no final judgment be entered upon the claims reserved for further hearing and disposition in paragraph 9.

2. It adjudged that the objectants have failed to establish any right to surcharge against the receivers of United Oil Producers Corporation or recovery against Middle States Petroleum Corporation in favor of the estate of United Oil Producers Corporation or any of those claiming through said estate.

3. It denied all motions for surcharge on the final report and final accounting of the receivers of United Oil Pro-

ducers Corporation "and said final report and final accounting are judicially approved and settled."

4. It discharged Joseph P. Tumulty as a receiver of said United Oil Producers Corporation.

5. This paragraph reads: "The motion for discharge of Joseph Glass, as a Receiver of United Oil Producers Corporation, is denied without prejudice to renewal thereof on determination of the other final accountings of all the receiverships in this cause, after presentation to the Court for decision on notice to the Objectants and to all other non-depositing stockholders and creditors, of all the unresolved controversies referred to in paragraph 9 below, or existing between any of the receiverships in this cause or between any of such receiverships and Middle States Petroleum Corporation."

6. It dismissed on the merits objectants' general charges of fraud and conspiracy.

7. It dismissed on the merits objectants' specific claims of fraud and conspiracy listed in said paragraph.

8. It dismissed the cross-claim of Middle States Petroleum Corporation against the executors of William W. Cohen, deceased "on the ground that it is barred by the applicable New York statute of limitations."

9. It reserved for further hearing and disposition eight matters listed in said paragraph.

Although the parties did not raise the question of the appealability of the order this court is constrained to do so. The discharge of Tumulty as receiver (paragraph 4) and the dismissal of Middle States' cross-claim (paragraph 8) are a final disposition of those matters. But obviously issues raised by the objectants with respect to the discharge of Joseph Glass as receiver have not been finally deter-

BLEED THROUGH POOR COPY

mined. Whether the further hearing on the matters reserved results in surcharge or discharge of him as a receiver of United Oil, the losing party may then appeal from that order. In a case so complicated as this it would be extraordinarily wasteful of judicial effort, on the part of both court and counsel, to decide on the present appeal the issues with respect to paragraphs 4 and 8, and then on a later appeal have to traverse the same ground again with respect to Glass as receiver. We are unwilling to do so.

It may be avoided in either of two ways. One way is to adjourn the present appeal until the District Court shall have completed hearings on the matters reserved and, if an appeal is then taken, it can be consolidated with the present appeal. The second method is for the appellants to stipulate that the decree shall be considered to be modified so as to add to paragraph 4 the name of Joseph Glass as receiver, and to delete paragraphs 5 and 9. If the parties so desire, they may file such a stipulation with the Clerk of this Court within 15 days. Otherwise the appeal will be continued to await final disposition of the matters reserved by the District Court for further hearing.

REPORTED IN 210 FED. (2) 360

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 128—October Term, 1952.

(Argued March 15, 1953 and October 28, 1953

Decided January 15, 1954.)

Docket No. 22426

JOSEPH A. PHELAN,

Complainant,

—v.—

MIDDLE STATES OIL CORPORATION, *et al.*,

Defendants.

Before:

L. HAND, SWAN and FRANK,

Circuit Judges.

Appeals from the United States District Court for the Southern District of New York, J. Joseph Smith, *Judge.*

Meyer Krashaar and Sophie D. Cohen, as sole surviving executors of William W. Cohen, deceased, Sophie D. Cohen, individually and Levy Bros., objectants to the final report and account of Joseph P. Tumulty and Joseph Glass as receivers of United Oil Producers Corporation, appeal from a judgment which adjudged that the objectants have failed to establish any right to surcharge against said

BLEED THROUGH POOR COPY

receivers or to recovery against Middle States Petroleum Corporation in favor of the estate of United Oil Producers Corporation, approved the final report and final accounting of said receivers, discharged Joseph P. Tumulty as such receiver, and denied a discharge to Joseph Glass as such receiver, without prejudice to renewal of his motion for discharge after the court shall have determined certain reserved issues. Middle States Petroleum Corporation has appealed from so much of the judgment as dismissed its cross-claim against the executors of William W. Cohen, deceased.

Appeal of objectants as to Glass dismissed; and as to other issues adjourned; decree reversed and cause remanded on appeal of cross-claimant.

KRAUSHAAR & KRAUSHAAR, *Attorneys for objectants-appellants:* Meyer Kraushaar, of Counsel.

JOSEPH P. TUMULTY and JOSEPH GLASS, *as receivers of United Oil Producers Corporation, pro se., appellees;* Leslie Kirsch and Joseph P. Tumulty, Jr., of Counsel.

SHEPPARD AND SEIPP, *Attorneys for Middle States Petroleum Corporation, appellee and cross-appellant:* Ralph Montgomery Arkush, of Counsel.

SWAN, *Circuit Judge*:

In *Phelan* v. *Middle States Oil Corporation*, 2 Cir., 154 F. 2d 978 this court reversed an order settling the accounts and discharging the receivers of United Oil Producers Corporation, and remanded the cause for further proceedings. Upon remand a lengthy trial was had before Judge Smith.

sitting in the Southern District of New York. The great number of detailed findings of fact and the length of his memorandum opinion show the extraordinary thoroughness and ability with which he dealt with a most complex situation. The judgment directed is now before us on the appeal taken by objectants to the final report and account of the receivers of United Oil Producers Corporation, and the cross-appeal of Middle States Petroleum Corporation. The judgment contains nine separately numbered paragraphs. A summary of each paragraph is set out in *Phelan* v. *Middle States Oil Corporation*, 2 Cir., 203 F. 2d 836, and need not be repeated here. In that opinion we held certain parts of the judgment not to be presently appealable, and suggested the possibility of curing the defect by stipulation. Thereafter, by stipulation the parties modified the judgment in the respects suggested.[1] However, subsequent study of the case caused doubt to arise in the mind of the court as to the effectiveness of the stipulation. Further argument regard-

[1] The stipulation reads as follows:

"It is hereby stipulated and agreed by and between the undersigned hereunto duly authorized:

1. That the decree shall be considered to be modified so as to add to paragraph 4 thereof the name of Joseph Glass as a receiver of United Oil Producers Corporation and to delete paragraphs 5 and 9 of the decree.

2. Objectants-appellants waive any objection and the right to make any objection to said decree upon the ground that, as so modified, it provides for the discharge of Joseph Glass as a receiver of United Oil Producers Corporation without requiring the prior determination of the final accountings in the receiverships of other corporations in this cause, and upon the ground that, as so modified, said decree is inconsistent with certain of the findings of fact, conclusions of law or opinion of the District Court.

3. Nothing herein contained shall be deemed to be an acquiescence by objectants-appellants in the discharge of said receiver of United Oil Producers Corporation."

BLEED THROUGH POOR COPY

ing appellate jurisdiction of the objectants' appeal was had on October 28, 1953.[2]

The parties urge that the judgment is appealable regardless of the amendment of paragraph 4 and the deletion of paragraphs 5 and 9 made by the stipulation. They say that the validity of the stipulation need not be decided. Their argument is that by virtue of paragraph 3, which overruled all motions to surcharge the receivers of United and approved their final report and accounting, and paragraph 4, which discharged Tumulty, the denial in paragraph 5 of a discharge to Glass without prejudice to renewal of his motion "on determination of the other final accountings of all the receiverships in this cause" was merely a postponement of his discharge, which will be granted as a matter of course, if, on the present appeal, this court affirms paragraph 3, because all of the issues reserved by paragraph 9 are irrelevant to United and its receivers. We think this argument confuses the correctness of the judgment with its finality.

[2] The order of July 22, 1953 (unreported) calling for such argument reads as follows:

> "In our former opinion, 203 F. 2d 836, we held that consideration of the appeal would have to be postponed until the District Court should decide the questions reserved unless the parties stipulated to modify the judgment in certain respects. Their stipulation was thereafter filed. In effect the stipulation would seem to be a dismissal or compromise of some of the issues reserved by Judge Smith for future decision. As the objectants have filed objections to the accounting of the receivers not only for themselves but also on behalf of all persons similarly situated, doubt has arisen as to the power of the objectants to bind by stipulation the other members of the class in view of Rule 23(c) F. R. C. P. or under the general law if that rule is inapplicable. Also, further study of the record has left the court in doubt as to the feasibility of passing on the judgment until some of the numerous reserved issues shall be decided. The court desires counsel to advise it as to which of the issues reserved in Paragraph 9 of the judgment are relevant to the present appeal; as for example, what are the issues covered by subdivisions (d) and (e) of that paragraph. A convenient time in October 1953 may be arranged with the Clerk of the Court for discussion with the Court of the above mentioned matters."

It may be that none of the questions reserved in paragraph 9 can affect Glass' liability as receiver of United and that final settlement of his accounts in the other receiverships will also have no effect upon it, and consequently Judge Smith erred in conditioning his discharge on determination "of all the unresolved controversies" reserved in Paragraph 9, "or existing between any of the receiverships in this cause or between any such receiverships and Middle States Petroleum Corporation." But obviously paragraph 5 did so condition it; and that was the intention of Judge Smith is plainly apparent not only from his opinion but also from his 4th conclusion of law.[3] In three specific instances the opinion declares expressly that Glass should not be discharged until the controversy under discussion is decided.[4] There can be no doubt that the court meant to hold open the discharge of Glass against the chance that something might be developed in the other receiverships that would require his discharge as a receiver of United to be conditioned upon a condition not yet decided. Whether it was right or wrong for Judge Smith to say that the event in the other accountings could have any effect upon Glass' discharge in the United accounting, that is exactly what he did say most clearly. The "finality" of a judgment does not depend on whether it is right but on whether it disposes of all the issues; it is as little "final" when it should have done so, as when it should not. We do not hold that it should have done so in the case at bar, but merely that it did not. Hence the order was not final in respect to the liability of Glass, and

[3] "4. The Court should not grant final discharge of Glass the receiver of one of some 39 corporations in receivership in this action where the same receivers have acted in all the receiverships, where the receiverships have been treated for many purposes as a unit, while unresolved controversies exist between some of the receiverships and a corporation, formed under a plan of reorganization of some of the corporations in receivership, in which the receiver Glass is substantially interested and of which he is the executive head."

[4] See Folios 436, 446, 489 of Appendix to Objectants-Appellants' Brief.

BLEED THROUGH POOR COPY

the appeal as to him can be sustained only if the attempt by stipulation to make it final is effective.

The next question is as to the applicability of Rule 23(c) of the Federal Rules of Civil Procedure.[5] If this rule is applicable, the stipulation requires the approval of the district court. The parties have argued that Rule 66 takes the case out of Rule 23(c).[6] We do not so interpret it. Rule 66 was amended, effective in October 1949, so as to omit from the second sentence the words: " * * * but all appeals in receivership proceedings are subject to these rules," and to substitute the words: "In all other respects the action in which the appointment of a receiver is sought or which is brought by or against a receiver is governed by these rules." The "other respects" are those that do not concern "The practice in the administration of estates by receivers." It is not impossible to consider a receiver's final accounting and discharge as part of the administration of his estate; but that seems to us a strained and improper construction. In our opinion "administration" means the receiver's dealings with the property, and the "practice" in such administration re-

[5] "Rule 23. Class Actions
* * *

(c) Dismissal or Compromise. A class action shall not be dismissed or compromised without the approval of the court. If the right sought to be enforced is one defined in paragraph (1) of subdivision (a) of this rule notice of the proposed dismissal shall be given to all members of the class in such manner as the court directs. If the right is one defined in paragraphs (2) or (3) of subdivision (a) notice shall be given only if the court requires it."

[6] "Rule 66. Receivers Appointed by Federal Courts

An action wherein a receiver has been appointed shall not be dismissed except by order of the court. The practice in the administration of estates by receivers or by other similar officers appointed by the court shall be in accordance with the practice heretofore followed in the courts of the United States or as provided by rules promulgated by the district courts. In all other respects the action in which the appointment of a receiver is sought or which is brought by or against a receiver is governed by these rules."

fers to orders he must get to allow him to dispose of the property, to spend money to protect it, to distribute it among the creditors or lienors, and the like. In short, the "practice" means the procedure by which he gets the power to do those things which an owner of the property would have without court authorization. It is only after he has "administered" the "estate" and wishes to get immunity from personal liability that he files his final accounting and brings the parties into court to assert any claims they may make against him personally on account of his administration. We doubt whether even his application for an allowance is a part of his administration, although it does determine how a part of the assets shall be distributed; but however that may be, and assuming that the former practice should apply to a receiver's application for an allowance, it is a separate question from deciding whether there are outstanding claims against him personally.

Moreover, if we look to the purpose of Rule 66 no reason is apparent for treating a receiver differently from other fiduciaries. If the Federal Rules of Civil Procedure govern the accounting of a trustee or an agent, we see nothing in the accounting of a receiver to require resort to a different procedure. If one of several beneficiaries having common rights who excepts to their trustees' accounting, may not dismiss his claim without the court's approval, we submit that it would be absurd to hold that an objector to a receiver's accounting should be allowed to do so. There is no necessity for observing local rules in such a case.

There remains the question whether Rule 23(c) applies to the situation before us. Does the stipulation "dismiss" an action? Plainly it does not "compromise" one. It does not dismiss the whole action, but it does dismiss any claims that may arise in the other receiverships and with which, under Judge Smith's ruling, Glass might be charged in his accounting in the United receivership. Every reason for preventing the claimant in an action under Rule 23(a)(3) from dismissing the whole action seems to us to be equally cogent

BLEED THROUGH POOR COPY

against his dismissing any of the constituent items of which the claim may be made up. It is true that a plaintiff must be allowed to manage his action as he wishes; but managing it is one thing, and surrendering it is another. Suppose an action where one of several beneficiaries of a trust, suing on behalf of all, charges the trustee with a number of dereliections; why must he not get the court's approval before he can be allowed to dismiss any one of the charges? We think he must. Therefore the stipulation is not effective to make the judgment final as to Glass' liability and before we can get jurisdiction as to this the judgment must be amended with the approval of the district court.

It is urged that assuming arguendo that the stipulation is ineffectual, paragraphs 2, 3, 6 and 7, which overrule objections to the receivers' account and judicially approve and settle it and deny recovery against Middle States Petroleum Corporation, are appealable both as against the receivers and as against Petroleum without regard to the stipulation which, in any event, does not touch those paragraphs of the judgment. In support of the argument counsel cite *United States Fidelity & Guaranty Co.* v. *Higgins*, 9 Cir., 41 F. 2d 739 and *Crites, Inc.* v. *Prudential Ins. Co.*, 6 Cir., 134 F. 2d 925, 929, reversed 322 U. S. 408. The first holds that a decree settling the account of an equity receiver and directing him to pay the amount found due is a "final" decree and conclusive on the rights of all the parties in interest, so that the trustee in bankruptcy of the defendant in the equity suit cannot afterwards surcharge the receiver with an item asserted to have been omitted from the account through inadvertence. In the *Crites* case, without discussion of appealability, the sixth circuit entertained an appeal from an order overruling objections to and approving a receivers' first and amended first accounts, and directing the receivers to file their final account covering the period subsequent to that covered by the approved accounts. Both cases are inapposite. In neither was a receiver denied a discharge until the court should determine issues reserved.

The judgment as it stands is final as to Tumulty but for reasons stated in our former opinion we are unwilling to decide his case apart from that of Glass. So far as the judgment is final in denying recovery against Middle States Petroleum, to review that part of the judgment before the parts which affect the receivers can be reviewed would be wasteful judicial administration. We think they should be reviewed at the same time. The judgment dismissing the counterclaim of Middle States Petroleum Corporation is also final, and the issues presented by the counterclaim are sufficiently distinct from the other issues to permit review of this part of the judgment at the present time. Though we must dismiss the objectants' appeal as to the liability of Glass, we will make the result as little onerous as possible. The parties may go before Judge Smith, if they so desire, and ask him to amend the judgment in accordance with their stipulation. If he approves, giving such notice to other members of the class as he thinks necessary, an appeal may be taken from the amended judgment, and the record will consist of the present record remaining on file in the court together with whatever further proceedings have taken place before Judge Smith. It would seem that the briefs now on file, supplemented if necessary by short additional briefs, would serve for the new appeal, and possibly the case could be decided without further argument if the parties so wish. Such details can be determined later.

The cross-appellant's counterclaim alleges that Cohen obtained $17,207.99 from Middle States Petroleum Corporation by fraud. The allegations were that on January 11, 1935 he presented United bonds of the face value of $32,000 for payment of the distributive value thereof, thereby representing that he was the owner of all of said bonds, whereas in fact $24,700 of them were owned by Reliable Securities Corporation; that relying on Cohen's representation of ownership Petroleum paid the depositary, who in turn paid Cohen, the distributive value of the $24,700 owned by Reliable; and that the fact of Reliable's ownership was not

BLEED THROUGH POOR COPY

discovered by Petroleum until a few days before the trial of the present accounting. Cohen's executors pleaded to the cross-claim a general denial and New York statutes of limitations. On April 18, 1951 Judge Smith directed judgment for the cross-claimant. The objectants moved for a rehearing, which was granted, upon the affidavits, exhibits and arguments submitted, without taking evidence orally in open court. On July 25, 1951 Judge Smith modified his prior opinion, findings of fact and conclusions of law, and dismissed the counterclaim on the ground that it is barred by the applicable New York statute of limitations.

Assuming for the moment that fraud by Cohen in cashing the bonds as his own was proven, or might have been proven on the rehearing had evidence been taken in open court, we shall first consider the court's ruling as to the statute of limitations. The question is whether when Petroleum cashed the bonds, that is, paid their liquidating value, in 1935, it had notice or ought to have had notice that the bonds did not belong to Cohen. The objectants, as we understand their argument, do not contend that Petroleum had an actual notice of Cohen's title beyond what may be inferred from his possession of them. Their argument rests on the claim that Petroleum is chargeable with such information as its president Glass had, and that Glass learned or should have learned of the fraud, if fraud there was, while he was receiver of Middle States Oil and its numerous subsidiary and affiliated corporations, and more than six years before the cross-claim was filed in 1948. In his memorandum opinion, after referring to evidence relating to the Reliable account, Judge Smith said:

> "We may conclude that Glass had at hand sufficient information to put him on inquiry as to the status of Reliable's account with Cohen. See Higgins v. Crouse, 147 N. Y. 411 (1895). And since M. S. P. is bound by the knowledge which was within the reach of Glass, it cannot now be heard to assert that it was unaware until shortly before the trial on the United accounting

of the alleged fraud in Cohen's implied representation that he was the owner of the U. O. P. bonds."

In supposing that the law of New York imputes to the principal the agent's knowledge under all circumstances the learned judge was in error. The rule is much more limited. A principal is not charged with his agent's knowledge obtained before he became an agent (or before he acted in the transaction), unless the information was in the agent's mind when he acted for the principal on the occasion under scrutiny. This rule taken over from English cases, was announced by Mr. Justice Bradley for the Supreme Court in the *Distilled Spirits Case*, 11 Wall. 356. It has been accepted without question by the Court of Appeals of New York in *Title Guarantee & Trust Co.* v. *Pam*, 232 N. Y. 441, 457 which cites not only the *Distilled Spirits Case* but also numerous New York decisions. Consequently we do not see how the statute could have run against Petroleum's cross-claim unless in 1935 when Cohen cashed the bonds, Glass had in mind the information which ought to have advised him of the infirmity in Cohen's title. Although Glass was then president of Petroleum, there is not the slightest reason to suppose, if he took any part in cashing the bonds, he then had in mind this information; indeed, there is no evidence that he took any part whatever in cashing the bonds, which was in any event only a part of the execution of the decree in the United receivership declaring what was the distributive value of its bonds.

The above discussion of the statute of limitations has proceeded upon the assumption that Cohen perpetrated a fraud. If the cross-claimant failed in a properly conducted trial to prove the fraud, dismissal of the cross-claim should be affirmed on the ground regardless of error in sustaining the defense of the statute of limitations. In finding 271(a) the court found that by presenting the bonds for payment of their liquidating value "Cohen thereby represented, as to all said 32,200 of United bonds, that he was a person intended

BLEED THROUGH POOR COPY

to be benefited by the decrees and entitled to such payment under the decrees" and "M. S. P., relying on said representations, made the payment received by Cohen." But in its memorandum opinion the court said (fol. 515), "* * * we cannot say that M. S. P. has borne the burden of establishing Cohen's bad faith in the presentation of the bonds." This conclusion was reached on the motion for rehearing which was decided upon affidavits, exhibits and arguments without taking evidence in open court. The cross-claimant objects to this procedure. He contends that Rule 43(a) of the Federal Rules of Civil Procedure requires that "In all trials the testimony of witnesses shall be taken orally in open court unless otherwise provided by these rules * * *" ; and that Rule 59(a)(2) which authorizes the court to change the findings and judgment and to enter a new judgment, contemplates modification of a judgment in favor of the prevailing party rather than giving judgment, without a retrial, to the losing adversary.[7] Where the motion raises only a question of law, we have no doubt that Rule 59(a)(2) permits a court to reverse completely its prior judgment and give judgment for the other party, if the evidence taken at the trial justifies it. But where new facts are presented in support of the motion for a rehearing, we think that normally at least there should be a trial of those facts before a judgment based on them is entered in favor of the movant. In the case at bar counsel for the movant stated by affidavit that he had in his possession "a file containing among other material," documents which he submitted as exhibits in support of the motion for rehearing. Similarly Mr. Matts selected from "a pile of old records" exhibits which he thought "pertinent." Conceivably, had a new trial been granted as to the issues raised by the cross-claim, the cross-claimant might have been able to require the production of all the records in the possession of these affiants and might have discovered other documents more favorable to

[7] See *Brooks Bros.* v. *Brooks Clothing of California*, D. C. S. D. Cal., 5 F. R. D. 14, 15-16.

its case than those picked out by them. Upon the original trial the court had sustained the cross-claim; the new evidence submited by affidavit caused the court to change its judgment. Proof of Cohen's fraudulent intent, particularly after his death, was difficult to make at best. We think the cross-claimant is entitled to have the evidence which produced a change in the judgment tested by trial in open court. We are not certain that the cross-appellant desires a new trial. Despite its argument that "the decision should not have been reversed without at least a partial new trial," the final point of its brief is that "A new trial of the cross-claim is not required." For reasons already stated we think the cross-claimant is entitled to a new trial if it desires one. In view of this conclusion we refrain from expressing an opinion as to the sufficiency or insufficiency of the evidence taken at the trial to sustain the charge of fraud perpetrated by Cohen on the cross-claimant.

Accordingly the objectants' appeal in so far as it relates to Glass is dismissed; dismissal of the cross-claim of Middle States Petroleum is reversed and the cause remanded for further proceedings in conformity with the foregoing opinion; and in all other respects the appeal is continued for further hearing upon the record now on file and such supplemental record of further proceedings, if any, in the District Court as may hereafter be filed.

BLEED THROUGH POOR COPY

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

October Term, 1952.

(Petition filed January 28, 1954 Decided February 8, 1954.)

Docket No. 22426

JOSEPH A. PHELAN,

Complainant,

—v.—

MIDDLE STATES OIL CORPORATION, *et al.*,

Defendants.

Before:

L. HAND, SWAN and FRANK.

Circuit Judges.

On petition for rehearing of so much of our judgment of January 15, 1954 as reversed dismissal of the cross-claim and remanded the cause for further proceedings.

MEYER KRAUSHAAR, *Attorney for Petitioners.*

PER CURIAM:

The petitioners have convinced us that our opinion was in error in stating: " * * * indeed, there is no evidence that he [Glass] took any part whatever in cashing the bonds, which was in any event only a part of the execution of the decree

in the United receivership declaring what was the distributive value of its bonds." This statement is withdrawn.

We adhere to our ruling as to reversal and remand on the cross-claimant's appeal but wish to make it plain that on the retrial both the issue of fraud and the defense of the statute of limitations will be open. Either party may add to his case not only on the fraud issue but also on whether at the time when Glass provided funds with which to pay the distributive value of the bonds he had in mind any information which required him to examine into Cohen's ownership of them. On the latter issue nothing said in our former opinion is to be construed as holding contrary to the petitioners' contention that the burden of proof is upon the cross-claimant.

Costs on the cross-claimant's appeal are awarded to the cross-claimant. The respective claims as to amount of such costs may be submitted to the Clerk of the Court.

BLEED THROUGH POOR COPY

REPORTED 154 FED. (2) 978

UNITED STATES CIRCUIT COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 214—October Term, 1945.

(Argued February 15, 1946 Decided March 21, 1946.
Opinion revised and rehearing denied, April 16, 1946.)

Docket No. 20068.

[SAME TITLE.]

Before:

SWAN, CLARK and FRANK,

Circuit Judges.

Appeal from a denial of a motion and an order made by the United States District Court for the Southern District of New York. Reversed and Remanded.

KRAUSHAAR & KRAUSHAAR (Meyer Kraushaar and David I. Kraushaar, of counsel) for appellants;

JOSEPH P. TUMULTY and JOSEPH GLASS, as Receivers of United Oil Producers Corporation, *et al.*, *pro se* (Joseph Glass and Leslie Kirsch, of counsel);

SHEPPARD & SEIPP, for Middle States Petroleum Corporation (John S. Sheppard, of counsel).

Middle States Oil Corporation, a holding company, and its subsidiary and associated companies were, until 1924, dominated by one Haskell.[1] In June 1924, this "system" faced serious financial difficulties. At about that time, Shivers, Haskell's secretary, went to Paris, France. At about the same time, Haskell sent the books of Middle States to Paris. Soon thereafter Shivers, as a stockholder of Middle States, filed a stockholders' bill against that company in the court below, praying the appointment of a receiver. Shivers' attorney in this suit was Joseph Glass who signed the bill as counsel. Glass also assisted in the formation of a Middle States stockholders' Committee headed by one Fleming who continued as its chairman, until the reorganization described below, and who also became a member of the reorganization committee.

The appointment of a receiver in the Shivers' suit was vigorously resisted and none was appointed therein. In August 1924, a "friendly" creditors' equity suit was instituted in the court below against Middle States in which, on the basis of the usual answer by the defendant, the court appointed Joseph P. Tumulty and Julius M. Mayer as receivers. Glass was appointed as one of the attorneys for the receivers. In a short time, the receivership was extended to thirty-six other companies in the "system." These receiverships were consolidated in the proceedings as thereafter conducted.

Among these companies were United Oil Producers Corporation, Imperial Oil Corporation, Eureka Producing Company and Turman Oil Company. Of the stock of United, two-thirds was owned by Imperial and the balance by Middle States which in turn owned some 97% of the stock of Imperial. United owned all of the stock of Eureka, and Eureka owned some 82% of the stock of Turman. An-

[1] See Cardozo, J., in *Marr* v. *Tumulty*, 256 N. Y. 15, for a comment on the "mazes" of but a portion of this holding company structure.

BLEED THROUGH POOR COPY

cillary receivers were appointed for the physical properties in jurisdictions in which those properties were located. On January 27, 1926, Mayer died and Glass was appointed in his stead as one of the two receivers in all those receiverships pending in the court below.

United had outstanding publicly-held 8% negotiable bearer bonds in the face amount of $2,439,900. Pursuant to a trust indenture, these bonds were secured by the pledge of all the Eureka stock. As stated more in detail below, pursuant to decrees of foreclosure sale and confirmation entered in 1929, and in accordance with a reorganization plan, the Eureka stock and all other assets of United were acquired in January 1930 by a new company of which Glass soon became president. But the United receivers were not discharged nor did they file their final accounts until some fifteen years later, in 1945.

The manner in which this "system" had been managed before the receivership left its inter-corporate finances in of said subsidiaries as between themselves. It will take actors' bill: "It has further been the general custom of Middle States, when it or one or more of the subsidiary companies required funds, to provide the necessary money out of the funds collected on account of subsidiaries as aforesaid, lending moneys collected on account of one subsidiary to one or more of the other subsidiaries as the money was required, in carrying on their operations. It was likewise the custom of Middle States to use said moneys in the payment of dividends which were declared from time to time by it or some of said subsidiary companies. In the handling of all of said funds as aforesaid, the same were not kept segregated as the funds of individual subsidiary companies, but were kept in a general fund by Middle States and disbursed practically as though said subsidiaries were all departments of a single corporation. In making disbursements on account of itself or for the account of said subsidiary companies, the funds used were taken from a general fund, except in a few instances where bank accounts were kept in

the names of subsidiary companies, and in such cases, funds were customarily transferred from one of said accounts to the other, as the occasion demanded or as the needs of the business might render advisable. In handling said funds as aforesaid, Middle States did not keep complete records or books of account which would show in detail the amounts of money which would be properly credited to said subsidiary companies, or the amounts with which said subsidiary companies should properly be charged. Neither did Middle States keep any complete books of account or records, wherein were segregated and charged to said subsidiary companies the amounts with which said companies should be properly charged as their proportion of the office and other administrative expenses of Middle States in carrying on and conducting the business of said subsidiaries as aforesaid. As a result thereof, the funds received by Middle States as the earnings of said subsidiary companies, have been intermingled, and the assets and business transactions of Middle States with said subsidiaries and the affairs of said subsidiaries among themselves have become seriously commingled, so that it will require a long, difficult and careful auditing of said amounts before the exact financial relations between the Middle States and said subsidiary companies and said subsidiary companies among themselves, can be accurately determined. On account of the situation above outlined, it is impossible now to determine whether Middle States owed said subsidiaries or whether they owe Middle States, and it is likewise impossible to determine the financial condition of said subsidiaries as between themselves. It will take accountants a considerable period of time to resolve all of said difficulties, and in the meantime, it is necessary, in order that the value of all of said properties may be preserved and their income undiminished, that they be handled practically as one property, being diligent, however, in keeping proper and correct books of account, so that each subsidiary company may finally receive for the benefit of itself and its creditors, all such funds and properties as may be equitably belonging to it."

BLEED THROUGH POOR COPY

In an affidavit by Glass dated April 4, 1944, he said: "The subsidiaries and their parent corporations were, prior to receivership, operated as a single business. They were honeycombed with advances and inter-company accounts. The practice of making advances from the subsidiaries to their parent corporations which antedated the receivership was continued by the Receivers, because the Receivers were under the necessity of operating the affairs of all the corporations as a single enterprise and it would have been impossible to operate otherwise. For those reasons this Court, in its order of October 23, 1924, early in the receivership, ordered 'that the business and properties of all the defendants should be administered as an entirety in this suit.'"

In reports filed in court by the receivers before 1929, they stated, inter alia, the following: The affairs of the companies "are so interwoven and so complicated" that the receivers "feel it to be their duty, through their familiarity therewith" to assist in formulating a reorganization plan; they had helped to organize a reorganization committee; but no reorganization fair to all interests could be prepared until there had been procured (1) estimates of valuations of the underlying physical properties and (2) adequate accounting data and balance-sheets because the books, records and accounts "were so incomplete, complicated and confused that it was impossible readily to ascertain approximately the financial condition of the companies or their true financial relation one to another." Accordingly, the receivers reported, they had employed valuation engineers to make detailed reports as to those values, and expert accountants to prepare correct accounts and balance-sheets. In a report dated April 11, 1927, Glass and Tumulty stated, that "much progress has been made in straightening out the records of the companies, and in reconstructing their accounts" but that "it is still impossible to present balance-sheets because of the state of flux that the valuations of the physical properties are in, until their values are definitely fixed in connection with income tax proceedings, and until

the government's allowances for depletion and depreciation are determined." They concluded this report with the statement that "the receivers will co-operate with all interests in their efforts towards an equitable and successful reorganization. They will lend such moral weight as comes from their position of disinterestedness, in support of such program of reorganization as seems most fairly to accomplish substantial justice to all of the interests involved. They will regard it as their duty to see, insofar as their efforts may be of any avail, that when the Court turns these companies back to corporate management, it will turn them back to directors and officials who will be truly representative of those whose interests are here at stake."

In a Third Report, filed on May 27, 1928—the last report filed before the reorganization—the receivers said "No schedule of intercompany claims is as yet presented. As hereinafter shown, balance sheets for all companies are now in process of completion, which balance sheets will show in detail the intercompany claim situation * * * Valuation engineers are now at work completing their appraisals of all of the leaseholds, producing and non-producing, owned by the several companies, as of December 31, 1927, so that a similar orderly record will be created of all acreage owned by the companies. The valuations thus arrived at will be used as the basis for proper book entries as of January 1, 1928, and for the first time during the corporate life of these companies an orderly accounting record of their affairs will be in existence. Balance sheets have been tentatively prepared with blanks left for the insertion of these figures derived from these inventories and valuations. In these balance sheets tentative treatment will be given to intercorporate accounts. It is the purpose of the receivers to thereafter present recommendations to the Court for the disposition, without litigation, of these intercorporate accounts upon notice to all interested parties. The valuations are expected to be completed in about 30 days. The receivers have two purposes in mind in the preparation of these in-

BLEED THROUGH POOR COPY

ventories, appraisals and balance-sheets, and in the installation of this accounting system. First, valuations and balance sheets are essential before any reorganization plan can be worked out. Second, the receivers feel it to be properly part of their duties to leave these companies, when they emerge from receivership, in an orderly condition, with their assets and liabilities known and listed and with their affairs in order. To bring such a condition about, from the lack of record and the chaos as to existing record which the receivers found when they took over the affairs of the companies, has been a mammoth task, the magnitude of which will never be realized except by those very close to the affairs of the companies. The major complications which were encountered and solved have been in a general way mentioned in the reports. The innumerable lesser complications which surrounded the affairs of these companies had to be similarly solved. The task has taken longer than was expected, but it is human experience that it takes much longer to untangle than to entangle. Fortunately, the end is in sight. The complications which remain are few in number * * * Reorganization has received serious consideration from the receivers, who have met from time to time with the Reorganization Committee organized at the suggestion of the receivers * * * The completion of the balance sheets, hereinbefore referred to, will enable the formulation of a definite program of reorganization * * * The receivers expect that their next report will be their final one."

But no balance-sheets or valuation estimates have ever been placed in the court files in the receivership proceedings. In their reports made of May 7, 1928, the receivers reported that oil leases on an eighty-acre tract in the Seminole field (Oklahoma) in which Turman owned a 5/8 interest had suddenly yielded immensely large and valuable production; that the receivers had rejected an offer on the basis of $2,000,000 for the entire working basis; that further expenditures on that tract had expanded the production; that Turman "shows an operating income of $1,280,765.54 in

1927"; that as a consequence there "has been a very substantial increase in the value of the security behind" the United bonds. The receivers said: "The oil industry has passed through a period of very severe depression since the last report, a condition which, while it still exists, appears now about to change for the better. Fortunately, by reason of the Seminole development, the Middle States companies have been able to survive this period and to emerge in better condition than they ever have been during receivership —with complications practically removed and with increased bank balances, increased acreage and increased production." [1a] But neither then nor later, in any report or other document filed in court, did the receivers give their own or the engineers' estimates of the value of the Turman properties.

On July 29, 1929, there was published a plan of reorganization agreed upon by committees representing certain holders of securities and claims against Middle States and certain of its several companies. This plan contained no balance-sheets or statements of inter-corporate accounts or valuation figures, although it stated, "Over 82% of the capital stock of Turman Oil Company, which is the most successful and owns the most productive properties of all of the subsidiary and Associated Companies, is owned by Eureka Producing Company, 100% of the capital stock of which is pledged as security for the U. O. P. Bonds."

The plan provided for a new company which, through judicial sales, was to become the owner of the assets of United (including the Eureka stock free of liens), of Imperial, of Middle States, and of Oil Development Company (another associated company). It was to have an issue of bonds and two classes of stock, A and B. The stock was to be deposited in a ten-year voting trust, the voting trustees to be named by the reorganization committee. United bond-

[1a] The receivers further reported that "claims against the companies aggregating $1,808,033.93 have actually been paid off out of income during receivership."

BLEED THROUGH POOR COPY

holders depositing under the plan were to receive new bonds, and also A stock in a fixed amount for accrued interest; depositing bondholders of Oil Development Company were to be similarly treated; depositors of claims against Gulf Coast, another subsidiary, were to receive specified A and B stock; depositing Serial Noteholders of Middle States were allotted specified amounts of A and B stock; and depositors of shares of Middle States were to receive named amounts of B stock. The plan contemplated that holders of non-depositing United bonds would receive only their pro-rata share of the amount paid for United assets at the judicial sales thereof. No provision was made for any payment by Middle States or Imperial of anything owing from either of them to United or for any payment on Imperial's guaranty of the United bonds.

Printed in the plan as published was a letter dated July 29, 1929, signed by the receivers and addressed to the chairman of the reorganization committee, which, in part, read as follows: "While we are in no position to, and do not intend to, bind the Court by our expressions, we are happy to say that in our personal opinion, your Plan of Reorganization does accomplish substantial justice to all of the interests involved * * * The receivership has now lasted for five years. Conditions which are referred to in the reports of the receivers have necessitated the extended term of the receivership. During this long period the receivers have endeavored, not only to conserve the properties and business as they were at the beginning of the receivership, but within such limits as are imposed upon the administration of any receivership estate, to bring the productive capacity of the properties, the character and condition of the equipment, the competency of the managing and technical personnel, the state of the engineering and accounting records and the general tone of the whole organization to such a point that we could turn over the business with a feeling of satisfaction in our own record and confidence in the record to be expected of the reorganized company. We believe

that that point has now been reached. We see no reason for the continuance of the receivership and every reason for the prompt consummation of reorganization, which we strongly urge." The plan stated: "At the suggestion of the Receivers, representatives of the various classes of securities have been engaged for more than a year in negotiations looking toward a reorganization." To carry out the plan, it was necessary, through foreclosure, to sell the Eureka stock pledged to secure the United bonds. By October, 1929, the accrued unpaid interest on these bonds amounted to $2,067,407.82. The reorganization committee on behalf of the 94% of the United bonds, the holders of which had deposited under the plan, made the needed demand on the trustee under the United indenture. The trustee, thereupon, after demand for this interest which was not paid, accelerated the maturity of the bonds. The trustee then asked leave of the court to foreclose; the receivers not objecting, the court gave its consent. Foreclosure, in ancillary proceedings, soon followed, and a decree of sale of the Eureka stock was entered therein. The court also decreed the sale (separate from the sale of the Eureka stock) of all the "free" assets of the several holding companies in the system, i.e., United, Imperial, Oil Lease Development Company, and Middle States.

At the judicial sales on December 16, 1929 the reorganization committee was the sole bidder. No upset prices had been fixed. The court confirmed the sales by a decree entered December 24, 1929. Nothing in the record shows that any evidence was received by the court as to the propriety of the prices before entry of the confirmation orders. In accordance with the plan, all the assets acquired by the reorganization committee were transferred to the new company provided for in the plan. The prices paid for the Eureka stock ($1,450,000) and for the "free" assets of United ($200,000) yielded a sum which represented about sixty-eight cents on the dollar on the face of each non-depositing United bond. Holders of all but $53,600.00 face amount of

BLEED THROUGH POOR COPY

such bonds deposited them under the plan and received new securities in accordance therewith. United had no creditors other than its bondholders.

On March 3, 1929, the judge wrote to the receivers as follows: "* * * To the end that I may have first-hand knowledge of what the actual situation is as to the possibility of a reorganization, I am asking you and the representatives of the various committees to appear before me on Saturday morning, March 9th, at 10.30 o'clock for the purpose of discussing various features of the case * * *"

At a hearing on March 9, 1929, the judge said:

> "The Court: I think what I shall do with respect to that will be to have you come before me, and these various committees for a short period of time and report as to what you have worked out in the way of some tentative plan of reorganization. I would prefer that the various groups, if they can do so, would work together, and form their own committee, taking into account every interest that is involved in this Receivership, so that I will have a composite view of the entire matter. But I am very earnest in saying that I want action at the earliest possible date * * *"

On July 12, 1929, Glass wrote the judge as follows: "I am sending you herewith the original of the report of the Sub-Committee as finally adopted yesterday afternoon at a meeting of the full Reorganization Committee at my office. There are some changes as against the copy last furnished to you * * * If, prior to the Monday hearing I can be helpful to you in arriving at an understanding of the proposed plan and the factors entering into the adoption of its component parts and the effect it will have upon the position of the respective securities, I will, of course, be glad to attend before you, at your suggestion and convenience." On July 30, 1929, in answer to a letter not in the record, the judge wrote Glass as follows: "Thank you for your letter

of July 20th. I am glad to know that active steps looking to a reorganization of Middle States Oil Corporation are now being taken, and wish to express my appreciation of your aid in furthering the possibility of soon getting this case out of the court and the properties restored to their owners."

At a hearing on confirmations of the sales, the following colloquy occurred:

"Mr. Lehman: May I also, in connection with that, file petitions of the successful bidders in the three foreclosure cases and in the Phelan cause likewise asking for confirmation of the sale, referring to the proposed transfer to the new corporation which is to be organized under a plan of reorganization that is attached to the petition?

"The Court: All right; I will confirm those sales in each instance.

"Mr. Lehman: I also respectfully submit to your Honor proposed order of the confirmation of sale with the stipulation signed by all of the counsel in the causes consenting to the entry of orders substantially in the form now submited.

"The Court: This includes the approval of the reorganization plan, does it not, or—

"Mr. Lehman: The reorganization plan as such is not submitted to the Court for its approval, but the Court is made now for the first time officially acquainted with the reorganization plan by virtue of the fact that it is now attached to the petition of the successful bidder and as a step in the reorganization the property is to be transferred to the reorganized company.

"The Court: The only reason I desired particularly to be advised upon the record as to the exact request that I here made is that I have received from a man in Chicago, whose name has, for the moment, slipped my mind, an objection against any court action designed to

BLEED THROUGH POOR COPY

effectuate a plan of reorganization and I wish to have noted upon the record that the Court is taking no step which may be construed as an approval of the plan without having its attention directed to the protest that he has filed. Is there anything else?

"Mr. Lehman: No, sir, that is all."

According to an affidavit recently made by Glass, he became president of the new company on January 1, 1930, and has ever since held that position, while still remaining receiver of the several old companies.[1b] Among the directors of the new company are one of Glass' law partners, a former secretary of the old company's stockholders' committee who is a close friend of Glass, a member of the old company's noteholders' committee and two members of the reorganization committee. This same group have retained these offices since the reorganization, apparently through a voting trust.

Glass on February 18, 1930, wrote the new company formally accepting the presidency.[1c] On February 27, 1930, the judge wrote Glass as follows: "Receipt is acknowledged of your letter of February 26, enclosing a copy of your communication of February 18th, addressed to Middle States Petroleum Corporation in regard to your election

[1b] Except as to some companies as to which he was discharged before 1945; in the case of United, he was discharged by the order from which appellants have appealed.

[1c] In that letter he said he was accepting on the following condition:

"That in the event any situation should arise wherein there should be any conflict of interest between your company and any company in the Middle States group of companies of which I shall continue to act as receiver, I shall not, in any such situation, act on behalf of your company, but only as such receiver and in all respects subject to the order and direction of the Court which appointed me. I shall be absolutely free to determine for myself when such a situation exists. I shall be absolutely free to take a position antagonistic to your company with respect to any matter, if in my opinion or in the opinion of the Court which appointed me as such receiver the performance of my duties as such receiver requires it."

to the presidency of that company. In view of the understanding evidenced by your letter of February 18th, and the acceptance of its terms by the Company, I see no impropriety in the arrangement that has been consummated between you."

The record on this appeal contains no evidence of the fees paid Glass as receivers' counsel, or as receiver, and none of his salary as president. During the years 1924-1933, the receivers filed twenty-five quarterly accountings which were reviewed by a special master and approved by the judge; those accountings related to receipts and disbursements but did not include balance-sheets, statements of the inter-corporate financial relations, or valuations.

Article Sixth of the decree of sale as to the unpledged ("free") assets, entered November 22, 1929, provided that the receivers should file with the court clerk, not less than ten days before the sale, "a statement showing and describing as definitely as practicable * * * but in general terms," the assets of Middle States, Imperial, United, and Oil Lease Development Company, with the proviso that "said statement shall be advisory only, and nothing contained therein or omitted therefrom shall be binding upon any of the purchasers or shall release any of the purchasers or buyers at such sale, nor shall such statement constitute ground for release from any debt, liability or obligation because of any representation therein or omission therefrom." The notice of sale required by the decree stated that "for further particulars, including a more particular description of the assets to be sold, and of the terms of sale, intending purchasers are hereby referred to said decree and to the record in said cause and to the statement of said receivers to be filed with the clerk of said court as in said decree directed." The sale was set for December 16, 1929. On December 6, 1929, the receivers, purporting to comply with Article Sixth of the decree, filed a "Statement" relating to the four designated companies. The data therein, relating to Middle States, covered seven type-

BLEED THROUGH POOR COPY

written pages; that relating to Oil Lease, four pages; that relating to Imperial, three pages; and that relating to United, three pages. Typical are the pages relating to United, which, in their entirety, read as follows:

"Statement filed by Joseph P. Tumulty and Joseph Glass, Receivers, pursuant to Article Sixth of Decree * * * dated November 22, 1929.

UNITED OIL PRODUCERS CORPORATION

(1) List of Assets, as at Close of Business November 30, 1929

		Amount
Cash in Coupon and Sinking Fund accounts, approximately		$4,369.40
Capital stock of the following companies:		
Company	*Shares*	
Eureka Producing Company	1,000	
The above cash and capital stock are held as collateral by Chatham Phenix National Bank and Trust Company, as Trustee, under Trust Indenture dated July 25, 1921 for United Oil Producers Corporation Ten Year First Lien Gold Eight Per Cent and Participating Sinking Fund Production Bonds; final Decree dated November 15, 1929, orders sale of assets pledged under above indenture.		
Claim against State of Delaware for refund of franchise taxes paid,		87.50
Claim against C. N. Haskell—amount undetermined		

Claim against Unity Securities Corporation—amount undetermined.

Claims against members of Haskell Family—amounts undetermined.

Miscellaneous accounts receivable, securities and assets believed to be worthless and uncollectible. Failure of enumeration of such accounts receivable, securities, and assets not to be deemed for any purpose a waiver or abandonment of same.

Claims against various subsidiary and affiliated companies for post receivership advances, subject to proration as between the defendant companies, Republic Producing Company, M S O Oil Corporation and The Louisiana and North West Railroad Company, pursuant to further order of this Court, hereafter to be entered—amounts undetermined.

Intercompany claims against subsidiary and affiliated companies:

Middle States Oil Corporation	1,371,002.93
Reliable Securities Corporation	786,693.50
Imperial Oil Corporation	2,236,564.06

(2) Liens and Charges

United Oil Producers Corporation Ten Year First Lien Gold Eight Per Cent and Participating Sinking Fund Production Bonds; secured by 1000 shares of Eureka Producing Company capital stock, and interest and sinking funds in hands of Trustee, all owned by United Oil Producers Corporation; indebtedness established by Decree of this

BLEED THROUGH POOR COPY

Court dated November 15, 1929, in the amount of $4,501,307.82 and interest; said Decree orders sale of assets pledged under Trust Indenture for above bond issue.

(3) Claims for Federal and State Taxes

Undetermined tax liability, if any.

(4) Indebtedness of Receivers

Allowances to Receivers—to be fixed by order of this Court.

Allowances to Counsel for Receivers—to be fixed by order of this Court.

Allowances to Assistants to Receivers— to be fixed by order of this Court.

Allowances to Special Master—to be fixed by order of this Court.

Allowances to Counsel for all parties to this cause—to be fixed by order of this Court.

Allowances to Tax Counsel—to be fixed by order of this Court.

Mattison, Davey and Winters, Accountants—$12,296.23, and additions for work in process, all subject to order of this Court, and all subject to proration by order of this Court.

W. O. Ligon and Company, Engineers—$5,306.07, and additions for work in process, all subject to order of this Court, and all subject to proration by order of this Court.

Undetermined tax liability, if any.
Current office salaries and expenses.

Claims by various subsidiary and affiliated companies for post receivership advances, subject to proration as between the defendant companies in receiverships, Republic Producing Company, M S O Oil Corporation and The Louisiana and North West Railroad Company, pursuant to further order of this Court, hereafter to be entered—amounts undetermined.

EXECUTORY CONTRACTS OF RECEIVERS

None.

(5) EXECUTORY CONTRACTS

None.

Further information with respect to the foregoing may be obtained upon request at the offices of the Receivers, Room 1401, 170 Broadway, New York, N. Y.

JOSEPH P. TUMULTY AND
JOSEPH GLASS, RECEIVERS
By: JOSEPH GLASS
RECEIVER"

On December 9, 1929, a week before the sales, the receivers filed a petition with the court, to which they attached statements of intercompany claims as of December 31, 1928. On December 14, 1929, two days before the sales, the court, pursuant to this petition, made an order that these inter-corporate claims should be allowed in favor of or against the several companies but "subject to readjustment by further order of this court from time to time upon further showing of the * * * receivers * * * the court reserving jurisdiction for such purpose until final decree is entered, barring the assertion of further intercorporate claims by said receivers." Neither the court's order nor these statements of accounts contained balance sheets or valuation data. On May 8, 1930, after the assets had been

BLEED THROUGH POOR COPY

conveyed to the new company, the receivers petitioned for adjustments of these intercorporate claims, and the court approved such adjustments in an order again providing that, upon further application of the receivers, subsequent adjustments thereof might be made.

One William Cohen on March 27, 1930 deposited under the plan $11,000 face amount of United bonds and received new securities accordingly. At some unknown date, after the time for deposit had expired, he bought $32,200 face amount of undeposited United bonds. There is no evidence as to where these bonds were when he purchased them, where the purchase occurred, or who was the seller. Cohen presented these bonds for pro-rata payment and on January 11, 1935, received $22,433.10 thereon, that being the pro-rata share of the cash paid at the sales of the United assets. Receipt of this amount was stamped on the bonds, which Cohen retained.

Cohen died in October 1940, leaving a will under which his wife, Sophie D. Cohen, is the sole beneficiary; she, Meyer Kraushaar and Clarence Cone are the executors. Among Cohen's effects were the stamped, undeposited United bonds and certain shares of stock of two other companies in the Middle States system. Sophie Cohen individually owns shares of some of those companies and a certificate for a small amount of indebtedness of Middle States.

Cohen's executors tried to ascertain, for inheritance tax purposes, the value of the securities left by him. Learning of the receiverships and of the fact that no final accountings had been made, they tried for some time, but unsuccessfully, to obtain the desired information from Glass. After these efforts failed, they examined as best they could the voluminous receivership records, but without reaching a conclusion which satisfied them. Glass had told them that, because of war conditions, it was impossible to prepare the final accountings. In March 1944, the executors made a mo-

tion in the receivership proceedings below for a compulsory accounting by the receivers, charging irregularities and fraud in connection with the receivership. After receiving affidavits from them and Glass, the district judge, on September 5, 1944, filed an opinion saying that he would suspend decision on the charges but that the receivers must file their final accounts by February 1, 1945.[1d] On that day, the receivers filed separate final accounts for each of the companies in receivership. In their brief on this appeal, the receivers state, "The receivers' final accounting of United is brief and simple. It is merely a schedularized statement in proper accounting form showing disposition of all the assets of United in accordance with the terms of the above-described final decrees." The receivers took the position that Middle States and Imperial were insolvent when their assets were judicially sold, and that all the United assets had been transferred, pursuant to the court's 1929 decrees, to the new company. At the end of March

[1d] This opinion reads as follows: "The papers supporting, and in opposition to, the relief sought by the Executors of William W. Cohen, deceased, are voluminous, and so contradictory in their averments as to what has taken place in the administration of the affairs of the defendants that, in the absence of an accounting by their receivers, an intelligent disposition of the pending motion is almost, if not entirely, impossible. Furthermore, it may well be that testimony having to do with the values of some of the properties and other facts, will ultimately be required in order that a proper record may be before the Court. For these reasons (and I may add that it is my opinion that, so far as possible, these receiverships should be concluded at an early date), I shall presently grant such portion of the motion of the executors as asks that the Receiver file an accounting of their acts down to and including December 31, 1943. Having regard for the effort and labor that this will entail, I shall fix February 1, 1945, as the date on which the accountings shall be filed. When the accountings are before the court and accurate knowledge of what has been done is thus available, the advisability of granting further relief to the moving parties can further be considered, or, if the executors then wish to object to the accountings, or portions thereof, definite issues can be raised, and these, if such action seems desirable, can be sent to a Special Master for hearing and report, and perhaps, for determination."

BLEED THROUGH POOR COPY

1945, they moved for settlement of these accounts and for their discharge as receivers. An answer and affidavits were filed by the appellants. There they referred to figures obtained from balance-sheets as of December 31, 1929, constituting part of a federal income tax return filed by the receivers; this income tax return had become known to the movants only after they had made their motion in March 1944, and had not been put of record in the receivership. The movants alleged under oath: "That the consolidated balance-sheets of Middle States Oil Corporation and affiliated companies show that company had assets of $24,397,604.38 and that its liabilities, except for capital stock, amounted to $23,400,038.79, which, after deduction of unearned discount on bonds, leaves $1,321,116.59 equity for the stockholders of the corporation. These figures are of course presumptive evidence of the financial position of the company as of the date it was reorganized, unless it can be established that the asset figures were inflated, the burden of establishing which would of course be on the receivers, * * * That the same income tax report contains a consolidated balance-sheet of the Imperial Oil Company, which had specifically guaranteed the bond issue, and that company's assets are shown to be $4,884,618.90 and its liabilities, other than for capital stock, were $1,394,607.60, leaving $3,490,011.30 for the benefit of shareholders. Here too, the value of the assets is understated inasmuch as one of its subsidiaries was the Eureka Producing Company, which owned and controlled the Seminole Oil Fields and which stock was carried at less than its true value on the books of that company. That included in the said income tax report is likewise the consolidated balance-sheet of United, which was the original obligor on the bond, showing that that company had assets of $7,094,370.91, which assets were less than their true value by reason of the fact that it owned substantial interests in the Turman Oil Company, which was also interested in the Seminole Oil fields; that the liability of that company, aside from capi-

tal stock, is shown to be $3,679,715.76, less unearned discount of $323,551.00, leaving net assets of $3,738,206.15 for shareholders, so that in any view of the case these companies were fully solvent." Glass, in a reply affidavit, did not deny that these balance-sheets contained such figures but said: "The consolidated income tax balance sheets referred to by Mr. Kraushaar do not purport to show values. They were prepared for the specific purpose of reporting liability for income tax on statutory bases of cost of assets, subject to deduction from such cost for depreciation, obsolescence and depletion in accordance with the income tax laws. Inert cost figures on an income tax balance sheet have no relation to value or solvency. Particularly is that so in this case, where the cost figures represented the inflated book costs resulting from the notorious manipulations of the Haskells."

On April 10, 1945, the executors and Sophie Cohen individually made a motion that Louis Roth, an expert public accountant and lawyer employed by them, be allowed to inspect (1) engineering and accountant reports relating to the companies involved in the receiverships which, while the receiverships were active, had been procured by the receivers and paid for out of the receivership estates; and (2) the books of account and vouchers of the receivers.[2]

[2] Attached to this motion was an affidavit by Ross which read in part as follows: "I am now engaged in such investigation and from the documents and papers that I have been able to find and which I have already investigated, I believe that there is probable cause to justify an extensive investigation on behalf of the stockholders, bondholders and subsidiaries of the associated companies. As far as I have been able to apprehend, none of the accounts that have been filed on February 1, 1945, gives any information with respect to the physical assets of the companies and the disposition thereof. They all deal with various intangibles such as stocks, bonds and intercompany transactions. These cannot properly be evaluated without the background of an inventory of the assets as they existed at the time the receiverships were initiated and as they presently exist, except by a long period of examination and analysis with considerable assistance. Thousands of items are involved. I verily believe that much time and effort can be saved if I am afforded an

BLEED THROUGH POOR COPY

The data to which the movants sought access had never been filed in court, and without a court order are not available to the movants. In an affidavit filed by Glass in opposition to this motion he referred to "the danger of making" this information available to them.

On July 27, 1945, the court filed an opinion reading as follows: "As a matter of right and justice, and also in the interests of good administration, I think it should here be ruled that Meyer Kraushaar, Sophie D. Cohen and Clarence Cone, as Executors of the Last Will and Testament of William W. Cohen, deceased, are without standing to object to the final report and accounting of Joseph P. Tumulty and Joseph Glass, as Receivers of United Oil Producers Corporation. My reason for this conclusion is that objectants' decedent had full knowledge of what was done in 1929 with respect to the assets of that company. He also had complete appreciation of the significance thereof. Instead of then objecting to this Court's disposition of the assets, he deliberately participated in the distribution of their proceeds. He first did this on March 27, 1930, and he did so again on January 11, 1935. Mr. Cohen lived until October 12, 1940. He had, therefore, a period of about ten years within which he might have assailed the decrees that are now under attack. Throughout all that time, neither he, nor any other creditor of United Oil Producers Corporation, sought to question the propriety of what took place in 1929 and 1930. Meanwhile, many parties, both individual and corporate, in reliance upon the integrity of what was then decreed, have acquired vested rights in the property formerly owned by the United Oil Producers Corporation. These rights, it seems to me, should not now, unless for compelling reasons, be disturbed. This is particularly so when the charges of fraud and chicanery that

examination of the original reports of Coverdale & Colpits, the engineers who originally made inventories and appraisals for the receivers, and the annual reports of Mattison & Davey, the certified public accountants who were retained by the receivers."

are presently made against the Receivers are wide in scope, and more or less indefinite in character. If, in the present condition of the pleadings, the objectants' allegations were to be sent to a Special Master for hearing and report, the proceedings would be long, tedious and highly expensive. Before authorizing a proceeding of this nature, and one which, in my opinion, would result in futility, I think that the Circuit Court of Appeals should be afforded an opportunity to pass upon the question as to whether the objectants, by reason of Cohen's acceptance of benefits under the decrees, should now be permitted to question the validity of transactions with which he was completely satisfied. In the light of these considerations, I shall approve the report of the Receivers and deny the objectants' motion to inspect the papers in their possession."

In accordance with this opinion, the judge on July 27, 1945 denied the motion; at the same time he entered an order settling the accounts of Glass and Tumulty as receivers of United and discharging them as receivers thereof and their sureties. From the denial of that motion and that order Sophie Cohen individually and the Cohen executors bring this appeal.

FRANK, *Circuit Judge:*

1. Because of the brevity of the district judge's opinion and because he made no findings, we have been obliged, arduously, to gather the pertinent facts from the parties' affidavits and those portions of the voluminous receivership records presented to us by the parties on this appeal. What we say of the facts should therefore be read with the understanding that they may appear to be very different after a further hearing in the court below. Necessarily, whatever comments we make on the basis of this incomplete record must be read as if they were written in the subjunctive mode. We are entering no final decision.

BLEED THROUGH POOR COPY

Since only in the United receivership was there an order discharging the receivers and approving their final accounts, our concern on this appeal is primarily with that receivership, the order denying access to the receivers' unfiled papers being interlocutory in so far as it affects the other receiverships. But we cannot, in our general survey of the facts, disregard what there went on. For appellee Glass, in an affidavit filed in the district court in opposition to appellants' motions, stated that the numerous companies "were, prior to receivership, operated as a single business," and "honey-combed with advances and intercompany accounts." He added that "the practice of making advances from the subsidiaries to their parent corporations which antedated the receivership was continued by the receivers"; that the receivers "administered [the companies] as a unity"; and that the plan "was consummated and the new parent company began to function on January 1, 1930, before the inextricably intertwined affairs of the subsidiaries and the old parent companies were straightened out by the receivers." [28]

2. Having in mind such cases as *Crites, Inc.* v. *Prudential Co.*, 322 U. S. 408, and others cited below, we think the general principles applicable here are as follows: A receiver, as "an officer or arm of the court," is a trustee with the highest kind of fiduciary obligations. He owes a duty of strict impartiality, of "undivided loyalty," to all persons interested in the receivership estate, and must not "dilute" that loyalty. He is "bound to act fairly and openly with respect to every aspect of the proceedings before the court * * * The court, as well as all the interested parties," have "the right to expect that all its officers," including the receiver, will not "fail to reveal any pertinent information or use their official position for their own profit or to further

[28] He added that this practice of "advancing the cash of subsidiaries necessary to carry on the business of the entire System" continued after the reorganization.

the interests of themselves or any associates." [3] A receiver has the "affirmative duty to endeavor to realize the largest possible amount" for assets of the estate.[4] If he has vital information which, if disclosed, might bring a better price for property which is sold pursuant to court order, he must fully disclose it "prior to the sale when the prospects [are] greater for successful bargaining." [5] Since failure to make such full disclosure has "a tendency to dampen the sale," [6] it is presumed that it did so, where the receiver had an interest in the sale in conflict with that of any other parties to the proceeding, "regardless of whether it actually had an adverse effect or not," because "the incidence of a particular conflict of interest can seldom be measured with any degree of certainty." [7] A decree confirming such a sale does not exculpate the receiver.[8] When the receiver has brought about such a sale, and the property after the sale has been transferred to a company in which interests of innocent third persons have become vested, usually the sale will not be set aside if there is available the more practicable method of surcharging the receiver for the difference between the price paid and the value of the property.[9] Where a receiver has a possible

[3] *Crites, Inc.* v. *Prudential Co., supra; Woods* v. *City Bank Co.*, 312 U. S. 262, 263.

[4] *Jackson* v. *Smith*, 254 U. S. 586, 588.

[5] *Crites, Inc.* v. *Prudential Co., supra.*

[6] *Ibid.*; cf. *Button* v. *Cities Fuel & Power Co.*, 300 Fed. 280, 299, 301 (C. C. A. 4), cert. den. 266 U. S. 619; *Investment Registry* v. *Chicago & M. E. Ry. Co.*, 212 Fed. 594 (C. C. A. 7).

[7] *Crites, Inc.* v. *Prudential Co., supra; Woods* v. *City Bank, supra; Jackson* v. *Smith, supra;* cf. as to trustees generally, *President & Directors of Manhattan Co.* v. *Kelby*, 147 F. (2d) 465, 476 (C. C. A. 2); *Restatement of Trusts*, § 170, comment c.

[8] *Crites, Inc.* v. *Prudential Co., supra;* cf. *Pangburn* v. *American Vault, Safe & Lock Co.*, 205 Pa. 93, 54 Atl. 508, 510; *Gutterson & Gould* v. *Lebanon Iron & Steel Co.*, 151 Fed. 72, 76-77.

[9] *Pangburn* v. *American Vault, Safe & Lock Co., supra;* cf. *Koontz* v. *Northern Bank*, 16 Wall. 196, 202-203.

BLEED THROUGH POOR COPY

personal interest adverse to those of any parties to the receivership, it is usually unwise for him to participate in the reorganization; if he does so he must act with unusual caution; that the court has acquiesced in his participating does not relieve him of his duty of disinterestedness.[10] A receiver who has strayed from his duty to the injury of anyone interested in the estate can and should be surcharged when he asks approval of his final accounting.[11] The rule that a receiver must not be motivated by personal considerations is prophylactic; its sanction is a surcharge.[12] A person interested in the estate who asks such surcharging is not barred because of laches if he acts with reasonable promptness after he discovers the facts showing such misconduct by the receiver.[13]

3. Just before these receiverships came into being, Glass had been the lawyer for stockholders of Middle States in a stockholders' suit against that company (a suit apparently still pending in the court below).[14] He thus repre-

---

[10] *Martin* v. *Luster*, 85 F. (2d) 833 (C. C. A. 7).

[11] *Crites, Inc.* v. *Prudential Co., supra.*

[12] *Woods* v. *City Bank, supra; Weil* v. *Neary*, 278 U. S. 160, 173; *Crites* v. *Prudential, supra; Jackson* v. *Smith, supra; Magruder* v. *Drury*, 235 U. S. 106, 119-120.

[13] *Crites, Inc.* v. *Prudential Co., supra*, at 417, note 8.

The surcharging is not limited to an amount measured by the interest of the particular person thus objecting to the receiver's accounting, since the surcharge is for the benefit of all similarly situated persons. For the court, in administering the estate in its custody for all the beneficiaries, must see to it that none of them suffers because of the misconduct of its receiver, and the discharge of that obligation should not depend upon their appearance in court to voice their objections to that misconduct. Cf. *Moon* v. *Wineman*, 57 Minn. 415, 59 N. W. 494, 495. Thus, if the judge learned of the misconduct from a wholly neutral source (cf. *Investment Registry* v. *Chicago & N. E. Ry. Co., supra*, at 608), he should surcharge the receiver and distribute among all interested the money owing to the estate by the receiver because of that misconduct.

[14] As late as June 1943, Glass' law partner asked the court not to dismiss that suit begun by Glass as counsel in 1924.

sented interests potentially in conflict with those of the United bondholders. For Middle States owned all the stock of Imperial, and directly and indirectly, all the stock of United; Eureka was wholly-owned by United; and Imperial had guaranteed the bonds of United. The Supreme Court has said that "the equity owner is peculiarly ill-suited to represent the mortgagee in those situations because of their historic clash of interests." [15] As the receiver of Middle States, of Imperial, of United and of Eureka, Glass should have been exceptionally vigilant to protect the interests of United bondholders whenever they conflicted with those of Middle States.[16]

We know, from the receivers' reports and from Glass' letter of July 12, 1929, that Glass, while receiver of these several companies, took an active part, in cooperation with the reorganization committee (the formation of which the receivers had brought about), in the formulation of the reorganization plan. The reorganization committee determined the prices to be bid at the judicial sale for the United assets by the committee, the only bidder at that sale. These prices fixed the pro-rata amount of cash required to be paid, as part of the plan and the decree, to those United bondholders who did not accept the new securities offered under the plan. There is need to enquire further in order to ascertain whether Glass—who worked closely with the committee [17] and was selected by it as the chief executive of the new company—had, in advance of the sale, agreed with the committee on those prices.[18] If he had, then he agreed that the non-depositing bondholders would be paid but sixty-eight cents on the dollar.

---

[15] *Woods* v. *City Bank*, *supra*.

[16] Cf. *Irving Trust Co.* v. *Deutsch*, 73 F. (2d) 121, 123 (C. C. A. 2).

[17] One of the members of the reorganization committee was the chairman of the stockholders' committee which Glass, in 1924, had helped to organize.

[18] Cf. *Tracy* v. *Willys Corp.*, 45 F. (2d) 484, 487 (C. C. A. 6).

BLEED THROUGH POOR COPY

The propriety of such a figure depended on such data, *inter alia,* as (a) the value of the Eureka stock, which in turn depended in part on the value of Eureka's physical assets, and (b) the worth of Imperial's guaranty of the United bonds, which, in turn, depended in part on the worth of Imperials and (c) the worth of United's claims against Middle States, which in turn depended on the worth of the securities and claims owned by Middle States, which in turn depended on the value of the physical assets owned by the divers subsidiary companies. In other words, to determine whether sixty-eight cents on the dollar was a fair amount to be paid to non-assenting United bondholders required a knowledge both of the values of the underlying physical properties of the underlying subsidiaries and of the inter-system accounting, and Glass, of course, so understood. In their reports filed before the sale in the consolidated receivership proceedings, the receivers had stated that they felt a moral obligation, stemming from "their position of disinterestedness," to ensure a reorganization fair to all interests. These reports had emphasized the fact that valuations of the properties were essential to such a reorganization. They had said the same of accurate inter-corporate accounting (including balance sheets)—and well they might, in view of the fact that the affairs of the companies (to quote Glass) were "honeycombed with advances and inter-company accounts." [19] In these reports the receivers had also stated that they were obtaining valuation reports from valuation engineers, and accounting reports from expert accountants. In their Third Report dated May 27, 1928—the last report made before the sales—the receivers said that the valuations "are expected to be completed in about 30 days," and that correct balance-sheets were nearing completion. They added that they felt it their duty "to leave these companies, when they emerge from receivership, with their assets

[19] See *Consolidated Rock Products Co.* v. *DuBois,* 312 U. S. 510

and liabilities known and listed and with their affairs in order."

But the receivers never filed in court the corrected balance sheets, or those valuation and accountants reports. Nor did the reports of the receivers themselves contain or reflect such information.[20] From them no one could tell the net worth of Turman or the worth of the Eureka stock or the value of United creditor claims against Middle States and other companies. Similar information was omitted from the reorganization plan; attached to it are a list of intercorporate stock ownerships, a statement of oil production, a "summary of net income from operations and application of cash receipts and disbursements," and a list of bank balances—but no balance sheets or valuations. As above noted, Glass conceded that "the plan was consummated and the new parent company began to function on January 1, 1930 before the inextricably intertwined affairs of the subsidiaries and the old parent companies were straightened out by the receivers." This plan, consummated in such conditions, contained a letter from the receivers stating that it "does substantial justice to all the interests involved" and urging its acceptance.

In the circumstances, we think that Glass assumed a peculiarly grave responsibility for the fairness of the treatment of non-depositing United bondholders. As a receiver—and especially as receiver of companies with potentially clashing interests—his obligations to the United bondholders were extensive. He stated that he felt it his duty to bring about a reorganization just to all interests; on the facts as they appear on this record he seems to have withheld from the court records information from

[20] Thus their Third Report contained only the following figures: (1) daily net oil production, (2) summaries of net income from operations and applications of cash receipts and disbursements, (3) claims filed and debts paid or disposed of during the receivership, (4) bank balances, (5) statement of acreage and production, (6) federal taxes, and (7) interrelated stock ownerships.

BLEED THROUGH POOR COPY

which each United bondholder might have formed his own independent judgment of value; and he aided in the formulation of a plan which omitted such information but which he recommended as fair to those bondholders. Accordingly, while on a full hearing it may seem otherwise, on the present record much is to be said for the proposition that Glass virtually underwrote the fairness of the amount paid to non-assenting United bondholders. He had, as receiver, "obtained inside information" [21] concerning the affairs of the several companies, the values of their assets, and the status of the intertwined accounts, and (so it seems on the record now before us) had communicated that information to the reorganization committee and to other committees but not to United bondholders individually. Under such conditions, no one other than the reorganization committee could intelligently bid at the sales.[22] True, the receivers' interim reports and the plan stated that Turman had become highly successful and that, accordingly, the Eureka stock, pledged to secure the United bonds, had increased very substantially in value. But, without valuation and balance sheets, such statements were too vague to be adequately informative to the United bondholders or to a bidder desiring to compete with the committee for the purchase of that stock. The same is true of the sales of the other assets; and the fairness of the prices those other assets brought may be pertinent if it appears that, had those assets fetched higher prices, something would have been realized for holders of United bonds on Imperial's guaranty or through debts of Middle States or still other of the companies to United.

Appellees make much of the fact that on December 9, 1929 (some four months after the plan was published and but a week before the sales), the receivers filed in court a proposed detailed statement of adjusted intercorporate

[21] Cf. *Martin* v. *Luster*, *supra*.

[22] Cf. *Button* v. *Cities Fuel & Power Co.*, 300 F. 280, 299, 301 (C. C. A. 4).

claims, and that on December 14, 1929, the court, on the receivers' petition, and on notice solely to the committees and to "the parties to the cause" (i.e., to the persons who had entered appearances) entered an order approving this statement.[22a] But this statement could not enlighten prospective bidders[22b] or non-depositing United bondholders (even if they had known of it), as to the worth of these claims, in the absence of balance-sheets and especially of valuation data; for the worth of a claim against a company obviously depends on the value of its assets. Moreover, the court order of December 14 approving these readjusted claims expressly left them "subject to readjustment" by further orders of the court upon further application by the receivers—an exceedingly elastic provision, which kept the status of the accounts uncertain, and of which the receivers availed themselves several months after the confirmation of the sales and the transfer of the assets to the new company. Here again we note, as markedly pertinent, Glass' recent affidavit to the effect that "the plan was consummated and the new parent company began to function on January 1, 1930, before the inextricably intertwined affairs of the subsidiaries and the old parent companies were straightened out by the receivers."

Appellees also make much of the following facts, said by them to demonstrate full disclosure to prospective bidders and to bondholders: (a) Article Sixth of the court's decree of sale relating to the "free" assets required the receivers to file with the court clerk on or before December 6, 1929 (ten days before the sale) "a statement showing and describing as definitely as practicable and made up to the latest day reasonably practicable, but in general terms" all of the assets to be sold, adding that this statement was to be "advisory only," and was not to be binding upon, nor should any accuracies therein release, a purchaser or bidder.

[22a] No published notice was given of the petition or of the court's order approving the statement.

[22b] The order approving it was made two days before the sales.

BLEED THROUGH POOR COPY

This decree also prescribed the form of the notice of sale, including a paragraph reading, "For further particulars, including a more particular description of the assets to be sold * * * intending purchasers are hereby referred to said decree * * * and to the statement to be filed with the clerk of the court as in said decree directed." (b) The prescribed notice of sale was published. (c) On December 6, 1929, the receivers filed with the clerk a "Statement" purporting to respond to Article Sixth of the decree. It consisted of seventeen typewritten pages. It contained facts as to Middle States, Imperial, Oil Development, and United; the facts as to Middle States covered three short typewritten pages; and those as to the other three companies, three such pages each. We quoted in full above, as typical, the portion dealing with United. It will be seen that it concludes with a sentence reading, "Further information with respect to the foregoing may be obtained upon request, at the offices of the receivers."[22c] Appellees maintain that this "Statement" was a full disclosure.

We cannot agree. The few pages dealing with United (which we take as typical) showed merely the following: the amount of cash in coupon and sinking fund accounts; the ownership of the Eureka stock; miscellaneous accounts receivable in undetermined amounts; three intercompany claims owing to United;[22d] the outstanding United bonds; indebtedness of the receivers, in unascertained amounts; and claims by other companies in the system "for post-receivership advances * * *—amounts undetermined." It contained no balance sheets and no valuation data; without such information, it was uninformative. The sentence with respect to "further information" did not meet the deficiency. For see: A person reading the published notice of sale

[22c] The statements as to each of the other three companies contained a similar concluding sentence.

[22d] This skeletonized statement as to intercorporate claims was even less adequate than the statement, discussed above, approved by the court on December 14, two days before the sales.

would find (as above noted) that it stated, "For further particulars, including a more particular description of the assets to be sold, and of the terms of sale, intending purchasers are hereby referred to said decree * * * and to the statement of said receivers to be filed with the clerk of said court as in said decree directed." If he had then read the decree, it would have told him virtually nothing he would want to know. If he went to the clerk's office and there read the "Statement" filed December 6, he would naturally suppose that it contained the vitally important facts intended to guide a prospective bidder. He would not normally believe that such important facts could be learned only by a request to the receivers (made within ten days before the sale) but would assume that any additional information thus obtainable by "request" would be relatively unimportant, marginal; for he would think that the receivers, presumably aiming to stimulate competition in the bidding, would reveal, in the Statement itself, what they considered the essential information helpful to potential bidders, since the decree had directed the filing of the "Statement" in order to advise such bidders. Why the receivers did not include the balance sheets and valuation reports (or summaries thereof) in their filed "statement of assets" is unexplained. On the record now before us, it would appear that they did virtually nothing to assist potential purchasers.[22e] However, on a further hearing, it may perhaps be shown that such was not the case.

Although the decree shows that the "Statement" was designed primarily for "intending purchasers," appellees urge that it should be regarded as also advising non-de-

[22e] Prospective purchasers of the Eureka stock—admittedly the most valuable asset of United—did not receive even the vague hint that "further information" might be obtained "on request" from the receivers; for the decree ordering the sale of that stock did not require the filing of any "statement of assets," nor did the published notice of that sale refer in any way even to the unsatisfactory "Statement" filed December 6.

BLEED THROUGH POOR COPY

positing United bondholders.[22f] We assume, arguendo, that it should. But how unenlightening the "statement of assets" would have been to any such bondholder, otherwise uninformed, we know from the fact that the receivers in their reports had previously said that correct valuations, when received by them, would be "used as the basis for proper book entries," making possible "for the first time * * * an orderly accounting record," and that "valuations and balance sheets are essential before any reorganization can be worked out." [22g]

To be sure, as appellees suggest, personal communication with non-depositing holders of United bearer bonds was not feasible. But, had the receivers desired to do everything practicable to inform such persons of the valuation data, they would have pursued the time-honored conventional course, i.e., they would have filed the balance sheets and valuation reports with the court clerk and then published a notice that they had done so. The receivers, in their brief and petition for rehearing, have as yet not adequately explained why they did not take these obvious steps but, instead, adopted a course which would make it least likely that any non-depositor would learn of the valuation data and balance sheets. Perhaps such an explanation will be forthcoming in the further hearings in the district court.

[22f] Appellees note that Cohen and his wife owned Oil Development stock; that the sales decree required the notice of sale to be mailed to stockholders of that company; and that that notice contained the sentence referring to the "statement of assets." Wherefore, say appellees, Cohen and his wife had notice by mail of the filing of that statement. Because of the insufficiency (discussed above) of that notice as adequate disclosure, we need not here consider whether, had it been sufficient, it would have served as notice to Cohen as a holder of non-deposited bonds.

[22g] What we said above as to the inadequacy of the "further information" sentence with respect to prospective purchasers applies as well to non-depositing bondholders.

Strikingly in contrast with the receivers' failure thus to inform non-depositing bondholders, is this fact, repeatedly asserted in appellees' brief: The receivers—without any special "request"—had furnished this very data (valuations and balance sheets) to the committees which formulated and endorsed the plan. As the plan was published July 29, 1929, this information had thus been given to the committee representing depositing United bondholders, more than four months before the receivers' "Statement" of December 6 was filed. Indeed, appellees seem to contend that this was the appropriate way of informing the non-depositors: They say that, because of these advices to the United bondholders' committee, "it is immaterial" that these data "were not placed in the court files" and they assert, repeatedly, that, as this committee, thus informed, approved the plan and the sales price, it must be assumed that the non-depositors received their due. In other words, appellees' position, in effect, seems to be that the receivers discharged their fiduciary duty, owing to all United bondholders, when they made full disclosure to the committee representing those who deposited. Of course, that is not true. The receivers represented all non-depositing as well as depositing claimants, but the committee did not. Fully to inform non-depositors was as much the duty of the receivers as to inform the committee. The very fact that no committee represented non-depositing United bondholders imposed on the receivers an obligation to keep them fully informed, to make essential information as easily accessible to them as was practicable.

Appellees, however, contend that all information obtained by the committee representing deposited United bonds must be imputed to Cohen. We here assume (without indicating possible qualification) that Cohen, in his capacity as a holder of deposited United bonds, and with respect to such bonds, must be treated as having had such knowledge "constructively." But, absent any proof that actually (not merely "constructively") Cohen had such

BLEED THROUGH POOR COPY

knowledge, we do not agree that it is to be imputed to him in his capacity as a holder of the non-deposited bonds, or to the person or persons who previously held those bonds.

That the United bond committee considered the plan fair to those whom it represented—persons who would accept the plan and receive new securities—did not at all mean that the treatment of non-depositors was fair.[22h] It was not enough that the plan be fair to those who accepted; it was also necessary that the sales price (in which alone the non-accepters would participate) should be fair. Equally necessary was it that the receivers make every feasible effort to see to it that individual bondholders who had not yet accepted be fully advised of all important facts, so that they could informedly decide whether or not to accept the new securities rather than their pro rata shares of the sales prices. On the record as we now have it, it would seem that the receivers came far from making such an effort.

With this background, we consider the charges made by appellants (charges, be it understood, that we do not accept as true on this incomplete record). They charge that Glass brought about the foreclosure of the United bonds and the sale of the Eureka stock, pledged as collateral therefor, in this way: That foreclosure could not have occurred except for the failure to pay overdue interest on the United bonds, with the resultant acceleration of their maturity and foreclosure by the trustee. But, say appellants, had Glass as receiver of United been safeguarding with undivided loyalty the interests of the United receivership estate, funds could have been obtained to pay that

[22h] Again and gain, appellees refer to the fact that the United bord committee represented holders of 94% of such bonds. But it is irrelevant that a large percentage of assenters approve of treatment unfair to non-assenters comprising a small minority. Cf. *Case* v. *Los Angeles Lumber Co.*, 308 U. S. 106, 115.

interest.[23] The values were such, say appellants, that had that default and the foreclosure been thus prevented, the bonds would ultimately have been paid in full. But, they charge, Glass did not pursue that course; instead, he allowed his other conflicting interests to dominate his judgment; and he wanted, for his personal financial advantage, to become president of the new company arising from a plan which (in order to meet the desires of security holders of Middle States and companies other than United) was contrived to the serious detriment of the non-assenting bondholders of United. To that end, it is charged, colluding with the reorganization committee, he deliberately failed to take steps to pay the interest on the United bonds. He also agreed, say appellants, with the committee, to a price at which the Eureka stock was to be and was sold at the judicial sale, a price far less than its fair value, Glass' failure to put of record the valuation and full accounting data before the sales must be presumed, appellants maintain, to have chilled the bidding, for only the reorganization committee, which bought at the sales, knew what the assets were worth. Because of the agreement that he was to be the new company's president, Glass, argue appellants, "was under a double duty to make complete disclosure of the true value of the assets to be sold; he was thus in the position of being a purchaser at his own sale."[24]

Moreover, say appellants, the United bondholders—both those who took new securities offered in the plan and those who instead took their pro-rata share of the cash bid at the sales—were justified in relying on Glass in the belief that they were receiving all to which they were entitled, because they justifiably relied on his assurance that the plan was fair to them; and that assurance, as to those who did not

[23] Whether that is true requires a knowledge of the kind previously outlined, i.e., a knowledge of the inter-corporate accounting and of the values of the physical properties in the system.

[24] Cf. *Restatement of Trusts*, § 170, comment c; *Tracy* v. *Willys Corporation*, 45 F. (2d) 485, 487 (C. C. A. 6).

BLEED THROUGH POOR COPY

deposit under the plan but took their share of the purchase price, amounted to an assurance that foreclosure was unavoidable and that the prices to be bid by the reorganization committee at the sales would be the best reasonably obtainable.

Postponing, for the moment, consideration of appellees' contentions as to estoppel and laches, we think that appellants' charges, on the facts now before us, have sufficient merit to require a full hearing in the district court. "That a trustee owes his beneficiaries undivided loyalty entirely untinged by considerations of any important benefits to himself is an old truth, and one whose edge cannot be dulled by frequent use. If the trustee here allowed its judgment to be affected by any such factors, it acted improperly. Cf. *Pepper* v. *Litton*, 308 U. S. 295, 311." [25] Because of his conflicting positions, the burden rests on Glass to show that the defaulted interest could not have been paid and that the prices at the sales were fair.[26]

---

[25] *York* v. *Guaranty Trust Co.*, 143 F. (2d) 503, 514-515 (C. C. A. 2, reversed on other grounds, 326 U. S. 99).

Chief Justice Stone has said that this principle embodies "the precept as old as Holy Writ, that 'a man cannot serve two masters' * * *. No thinking man can believe that an economy built upon a business foundation can long endure without loyalty to that principle." Stone, *The Public Influence of the Bar*, 48 Harv. L. Rev. 1, 8. In *Bayer* v. *Beran*, 49 N. Y. S. (2d) 2, 5-7, Mr. Justice Shientag said: "The fiduciary has two paramount obligations: responsibility and loyalty * * *. They lie at the very foundation of our whole system of free private enterprise and are as fresh and significant today as when they were formulated decades ago * * *. While there is a high moral purpose implicit in this transcendent fiduciary principle of undivided loyalty, it has back of it a profound understanding of human nature and of its frailties. It actually accomplishes a practical beneficent purpose. It tends to prevent a clouded conception of fidelity that blurs the vision. It preserves the free exercise of judgment uncontaminated by the dross of divided allegiance or self-interest. It prevents the operation of an influence that may be indirect but that is all the more potent for that reason."

[26] Cf. *Irving Trust Co.* v. *Deutsch*, *supra*, at 124. As to his burden with reference to the amount of damages, see *Bigelow* v. *RKO Pictures, Inc.*, ... U. S. ..... (February 25, 1946); *Package Closure Corporation* v. *Sealright Co.*, 141 F. (2d) 972, 979 (C. C. A. 2) and cases cited, *supra*, note 7.

The crucial question thus becomes this: Have appellants made out a prima facie case, not rebutted by appellees, that the values were as they assert? On that issue, appellants rely on the balance-sheets of United and Imperial as of December 31, 1929 (about the time of the reorganization) contained in income tax returns filed with the federal income tax officials by the receivers. Accepting the figures in these balance-sheets, United could have paid its bonds in full, and, if it could not, Imperial, guarantor of those bonds, could have met any deficiency. Appellees do not deny that the balance-sheets contain the figures as alleged by appellants. Nor have they offered any value data to contradict those figures. They contend, however, that, being but cost figures, they are not reliable evidence of value. But absent any other evidence, they do show a prima facie case,[27] certainly one sufficient to necessitate further judicial inquiry. Appellees have supplied no evidence to contradict this showing. It is relevant, in this connection, that the engineers' valuation reports and the accountants' reports have not been produced to rebut appellants' contentions; and it is not to be ignored that Glass, when asked by appellants to produce them, stated in an affidavit that there would be "danger" in making that information accessible to appellants—a curious position for a receiver to take, on his final accounting, concerning reports for which he paid out of the receivership assets, a position which cannot but raise a suspicion that such information would tend to substantiate, at least to a consider-

[27] *Heller* v. *Speier*, 119 Neb. 787, 230 N. W. 835; *Renick* v. *Dierks Lumber & Coal Co.*, 109 Neb. 300, 190 N. W. 875; *Miller* v. *Dilkes*, 251 Pa. 44, 95 Atl. 935; *Wesp* v. *Muckle*, 136 App. Div. 241, 120 N. Y. S. 976. See also, *Hinkel* v. *Motter*, 39 F. (2d) 159, 161; *Oberwinder* v. *Commissioner*, 147 F. (2d) 255, 259 (C. C. A. 8); *Cameron* v. *Commissioner*, 56 F. (2d) 1021 (C. C. A. 3); *Hurley* v. *United States*, 10 Fed. Supp. 365, 368.

That the figures in the income tax report are on a consolidated basis is not sufficient, absent countervailing evidence, to destroy their evidentiary worth.

BLEED THROUGH POOR COPY

able extent, the balance-sheet figures in the income tax returns.[27a]

4. Since appellants seek no relief with respect to the United bonds which Cohen exchanged for new securities under the plan, we need not consider whether that exchange would have barred appellants had they sought, with respect to those bonds, to surcharge the receivers. But we cannot agree that that exchange of those bonds prevents appellants, as successors of Cohen with respect to the unexchanged bonds, from thus seeking to surcharge.[28] As to those bonds, Cohen was in no different position from any other holder of undeposited bonds. There is nothing to show that he had better information than any other such holder; and no such holder, unless (unlike Cohen) he received special advice from the receivers or the committees, was informed of the data in the hands of the receivers as to values or (a related fact) as to the ability of the receivers to pay the interest on the United bonds.[29] Accordingly, as matters appear on the present record, appellants are not estopped, and are not guilty of laches.[30] They seem to have acted promptly when they recently obtained the income tax reports. Mere lapse of time, no matter how long, does not constitute laches: *Southern Pacific Co.* v. *Bogert*,

---

[27a] In the hearings to be held in the court below, in ascertaining values, attention should be paid to the earnings of the several companies. See *Consolidated Rock Products Co.* v. *DuBois*, 312 U. S. 510, 526-527.

[28] Cf. *Central Improvement Co.* v. *Cambria Steel Co.*, 210 F. 696, 710 *et seq.*, aff'd sub nom. *Kansas City Ry.* v. *Guaranty Trust Co.*, 240 U. S. 166.

[29] The record does not support the statement of the district judge that Cohen "had full knowledge of what was done with respect to the assets" of United and "also had complete appreciation of the significance there," if the judge meant that Cohen was informed of the values and accounting.

[30] Indeed, when appellants first charged Glass with misconduct, the judge said in an opinion that he would not hear them until the receivers had filed their final accounts.

250 U. S. 483; *Northern Pacific Railway* v. *Boyd*, 228 U. S. 482; *Holmberg* v. *Armbrecht*, ... U. S. ..... (February 25, 1946).[31]

Appellants do not ask (nor do they need to ask) that the decrees ordering or confirming the sale be set aside. They are not attacking the reorganization as such. They are seeking to hold Glass, as receiver, liable on the alleged ground that he misbehaved to the injury of his cestuis. It will not do to say that Glass merely obeyed what the court decreed, if on a full hearing it turns out that improperly he helped to bring about those decrees.[32]

The judge's guarded statement concerning the plan fell far short of its judicial approval. Nothing in the record substantiates appellees' assertion that he knew all about it; nothing indicates that, if it is true as appellants charge that the default in payment of the bond interest could have been averted or that the values were such that the prices at the sales were far below fair prices which would have been realized if full information had been supplied, the judge was aware of those facts. It is apparent that the judge—having had marked confidence in Glass' ability to preserve disinterestedness, despite the conflicting interests of the many estates of which Glass was receiver, and despite the fact that Glass came into the matter as a representative of Middle States stockholders—relied upon Glass' advice as to the inability to pay the interest and as to the adequacy of the prices.[33] If the facts as to values and as to

[31] See *Central Improvement Co.* v. *Cambria Steel Co.*, *supra*, at 713, where the Court said: "Laches is equitable estoppel under another name * * *." See also *Ferguson* v. *Wachs*, *supra*.

[32] See cases cited in notes 3 to 18a, *supra*.

[33] We may add that detailed information privately given to the judge would not necessarily estop those interested, to whom no disclosure was made, from asking that Glass be surcharged. This would be particularly true if the judge relied on Glass to translate for him the detailed data into summary form and Glass did so misleadingly.

BLEED THROUGH POOR COPY

Glass' alleged duplicitous conduct (which, if it occurred, was of course unknown to the judge) are substantially in accord with appellants' contentions, Glass cannot hide behind the judge's decrees or his approval of Glass' becoming president of the new company.[34]

Although appellees do not suggest it, the following argument might conceivably be advanced: The reorganization, in respect to United bondholders, violated the *Boyd* case principle [35] and this fact was apparent on the face of the plan; as neither Cohen's predecessor in title nor Cohen seasonably objected, the relief sought by Cohen's executors against Glass is barred even if he wrongfully assisted in consummating the plan. There are several answers to that suggestion. We mention but one: The *Boyd* case principle was violated if stockholders or creditors of Middle States, without adequate new consideration, received under the plan a participation in United assets and if United bondholders were not offered in the plan the equivalent of payment in full, since even the creditors of Middle States were not creditors of United but creditors of a stockholder of United. But, considering the lack of information in the court files and in the plan, no United bondholder not in the confidence of the receivers or of the committees could have discovered such a violation with sufficient ease to be on notice thereof. On this appeal, we do not deem it necessary to decide whether or not such a violation existed.

Appellants contend that it should be inferred that, before the sales, Glass had arranged with the reorganization committee to become the new company's president, or that he was influenced, when working with that committee, by

[34] *Martin* v. *Luster, supra; Gutterson & Gould* v. *Lebanon Iron & Steel Co.*, 151 Fed. 72, 76-77.

[35] *Northern Pacific Ry. Co.* v. *Boyd, supra; R. L. & P. R. R. Co.* v. *Howard*, 7 Wall. 392; *Louisville Trust Co.* v. *Louisville etc. Ry. Co.*, 174 U. S. 674; *Kansas City Terminal Ry. Co.* v. *Central Union Trust Co.*, 271 U. S. 445.

his desire to attain that position. As he was elected president soon after the reorganization,[35a] perhaps such an inference can be made; but we think that that fact should be determined, one way or the other, only after further evidence is adduced in the district court. We think, however, that, although such a fact would strengthen the case against Glass, it is not necessarily required to justify a surcharge.

5. Another argument based upon New York decisions (not suggested here or in the court below by appellees), we reject. According to those decisions, where a trustee, under an instrument securing negotiable bonds, has violated his duties but in such a way as not to involve a release or surrender of any trust assets, the right of action arising from the wrongdoing belongs to the persons who owned the bonds at the time of the commission of the wrong; and such a right, without an express assignment thereof, does not pass to a purchaser of any of the bonds, although the seller had no knowledge whatever of the trustee's dereliction.[36] On that ground, it is suggested that Cohen had no claim against the receivers and that therefore his estate has no standing here.

To this suggestion there are several answers: It is not entirely clear that the receivers' conduct, as it now appears

---

[35a] Glass, in his petition for rehearing, says that, in his affidavit, he mistakenly gave January 1, 1930, as the date of his election, but that the correct date is February 18.

[36] *Elkind* v. *Chase National Bank*, 259 App. Div. 661, aff'd 284 N. Y. 726; *Emmerich* v. *Central Hanover Bank & Trust Co.*, 291 N. Y. 570; *Hendry* v. *Title Guaranty & Trust Co.*, 225 App. Div. 497, aff'd 280 N. Y. 740; *Doyle* v. *Chatham & Phenix National Bank*, 253 N. Y. 369; *Smith* v. *Continental Bank & Trust Co.*, 292 N. Y. 275.

See discussion of these cases in *Brooklyn Trust Co.* v. *Kelby*, 125 F. (2d) 650, 653 (C. C. A. 2); *Elias* v. *Clarke*, 143 F. (2d) 640, 644 (C. C. A. 2); *York* v. *Guaranty Trust Co.*, *supra*, at 512; *President & Directors of Manhattan Company* v. *Kelby*, 147 F. (2d) 465, 474-475 (C. C. A. 2).

BLEED THROUGH — POOR COPY

on this record, did not constitute a release or surrender of assets within the meaning of the New York decisions.[37] Moreover, there is nothing to show that Cohen purchased these bonds in New York or that the bonds were in New York when he purchased them. Applying the New York rule of conflict of laws, the effect of a transfer of a negotiable instrument is determined by the law of the place where the instrument is at the time of transfer; see *Restatement of Conflicts*, § 349, and *New York Annotations* thereof (1935); cf. *United States* v. *Guaranty Trust Co.*, 59 F. (2d) 599, 801 (C. C. A. 2). In several other jurisdictions it has been held that a right of action for a tort to property, either real or personal, including a tort resulting from fraud, passes with the sale of the property to the purchaser although the seller does not expressly assign it; and, in cases not unlike the instant case, the federal courts, in pre-*Erie-Tompkins* days, so held.[38] These decisions are at odds with the apparent rationale of the New York decisions announcing the New York rule, i.e., that a mere assignment of a con-

[37] Glass, as receiver, had a fiduciary position with respect to the interest of United in the Eureka stock; he held the "equity"; and Glass, it is charged, colluded with the reorganization committee to bring about the default which led to the sale of that stock and at a price which was below its real worth.

As to the difficulty, under the New York decisions, of determining when wrongful conduct by a trustee involves a surrender of assets, cf. *President & Directors of Manhattan Co.* v. *Kelby*, *supra*, at 474.

[38] See, e.g., *Tracy* v. *Clews*, 115 U. S. 528, 539-541; *Comegys* v. *Vasse*, 1 Pet. 191, 213, 215-216; *Erwin* v. *United States*, 97 U. S. 392, 396; *Pattiz* v. *Semple*, 12 F. (2d) 276, aff'd 18 F. (2d) 955 (C. C. A. 7); *Zinn* v. *Denver Live Stock Commission Co.*, 68 Colo. 274, 187 Pac. 1033; *Rice* v. *Howard*, 136 Cal. 432, 69 Pac. 77, 81-82; *Emmons* v. *Barton*, 109 Cal. 662; *Sherman* v. *International Life Ins. Co.*, 236 U. S. 634, 639 (Mo.); *Billingsley* v. *Clelland*, 41 W. Va. 234, 23 S. E. 812, 820-821; *Scott* v. *Brazile*, 292 S. W. 185 (Tex.); 5 C. J. 892; 6 C. J. S. 1085-1086; 8 C. J. 387; 10 C. J. S. 690-691; cf. *Parkersburg* v. *Brown*, 106 U. S. 487, 503 (see p. 495 to the effect that the bonds were sold at 80¢ on the dollar); *Chapman* v. *County of Douglas*, 107 U. S. 348, 360; *Board of Commissioners* v. *Irvine*, 126 Fed. 689, 693-694 (C. C. A. 8); *Chelsea Savings Bank* v. *City of Ironwood*, 130 Fed. 410, 413 (C. C. A. 6).

tract usually does not carry with it a claim for a breach occurring before the assignment.[39]

For all we know, as the record now stands, the jurisdiction where the bonds were when Cohen purchased them was one which does not follow the New York doctrine. We have found no other jurisdiction in which that doctrine prevails, especially where a sale of negotiable instruments is involved. Since, then, this question of appellants' standing was not raised by appellees in the court below or even here, we should, if we considered the New York decisions applicable to a claim against a federal court's receiver, and if we concluded that there was here no surrender of assets, go no further than we have done in other similar cases, i.e., remand for ascertainment of the facts as to the location of the bonds at the time of Cohen's purchase.[40]

But we think that, with respect to the obligations of a receiver appointed by a federal court, the New York rule should not control. A claim against a derelict receiver is not against an ordinary trustee but against a court's officer. Who has the right to assert such a claim is a question affecting the integrity of the court itself.[40a] The federal courts, in holding their own officers to accountability, should not be hampered by state court decisions relating to ordinary trus-

---

[39] *Elkind* v. *Chase National Bank*, *supra*, at 666; *Hendry* v. *Title Guarantee & Trust Co.*, *supra*, at 500.

[40] *Benz* v. *Celeste Fur Dyeing & Dressing Corp.*, 136 F. (2d) 845, 848 (C. C. A. 2); *Nachman Spring-Filled Corp.* v. *May Mfg. Co.*, 139 F. (2d) 781, 787 (C. C. A. 2); *Zalkind* v. *Scheinman*, 139 F. (2d) 895, 904 (C. C. A. 2); *United States* v. *Rio Grande Dam & Irrigation Co.*, 184 U. S. 416, 423, 424; *Estho* v. *Lear*, 7 Pet. 130; *Armstrong* v. *Lear*, 8 Pet. 52, 74; *Security Mortgage Co.* v. *Powers*, 278 U. S. 149, 159, 160; *Pfeil* v. *Jamison*, 245 F. 119 (C. C. A. 3); *Wyant* v. *Caldwell*, 67 F. (2d) 374 (C. C. A. 4); *Columbus Gas & Fuel Co.* v. *City of Columbus*, 55 F. (2d) 56, 58 (C. C. A. 6).

[40a] Cf. *Mercoid* v. *Mid-Continent Investment Co.*, 320 U. S. 661, 671; *Hazel-Atlas Co.* v. *Hartford Co.*, 322 U. S. 238, 246.

BLEED THROUGH POOR COPY

tees.[41] When the United States issues a check, rights in that check (despite *Erie R. Co.* v. *Tompkins*, 304 U. S. 64) "are governed by federal rather than local law." *Clearfield Trust Co.* v. *United States*, 318 U. S. 363, 366-367. When a federal receiver incurs obligations through misconduct, the title thereto is, we think, similarly to be determined by "federal law."

What, then, is the "federal law" applicable here? In answering that question, we observe that the New York doctrine has this undesirable practical result: The seller of such bonds—*ex hypothesi* unaware, at the time of the sale, of the wrong done by the trustee—in actual fact can have no notion of retaining any cause of action against the trustee; and the seller of a bearer bond is exceedingly hard to trace. The practical consequence of the New York rule therefore is that most of the claims against a trustee for wrong done, especially to holders of bearer bonds, will never be prosecuted unless the trustee has surrendered trust assets. That rule thus often serves, pragmatically, as a convenient means of trustee exculpation.

We think that it would be most unfortunate to apply such a rule to a wrongdoing federal receiver; it would do much

---

[41] See, e.g., as to "federal law" in various fields. *Clearfield Trust Co.* v. *United States*, 318 U. S. 363; *Garrett* v. *Moore-McCormack Co.*, 317 U. S. 239; *Sola Electric Co.* v. *Jefferson Electric Co.*, 317 U. S. 173; *Prudence Realization Corp.* v. *Geist*, 316 U. S. 89; *United States* v. *Forness*, 125 F. (2d) 928, 937-940 (C. C. A. 2); *United States* v. *Pelzer*, 312 U. S. 399, 402-403; *Morgan* v. *Commissioner*, 309 U. S. 78, 80-81; *Lyeth* v. *Hoey*, 305 U. S. 188, 193-194; *American Surety Co. of N. Y.* v. *Sampsell*, ... U. S. ..... (Feb. 25, 1946); *Holmberg* v. *Armbrecht*, ... U. S. ..... (Feb. 25, 1946).

Many illustrations are given and discussed in Clark, *State Law in the Federal Courts*, 55 Yale L. J. (1946) 267.

We do not here consider the following suggestion: Restrictions on the bringing of stockholders' actions, such as those imposed by F. R. C. P. 23(b) or state statutes, are procedural; cf. *Piccard* v. *Sperry Corp.*, 120 F. (2d) 328 (C. C. A. 2, aff'g 36 F. Supp. 1006); *Galdi* v. *Jones*, 141 F. (2d) 984 (C. C. A. 2); *Towner-Hill Connellsville Coke Co.* v. *Piedmont Coal Co.*, 64 F. (2d) 817, 828 (C. C. A. 4, cert. den. 290 U. S. 675); the restriction imposed by the New York courts on suits by assignees of bonds is similar.

to thwart the policy of inducing careful discharge of their duties by receivers. The doctrine, relative to receivers, of strict accountability, and of opposition to divided loyalties, is prophylactic; it aims not merely to punish actual evil in cases where it occurs but to avoid the "tendency to evil in other cases." *Woods* v. *City Bank, supra; Weil* v. *Neary, supra; Crites, Inc.* v. *Prudential Co., supra; Jackson* v. *Smith, supra; Magruder* v. *Drury*, 235 U. S. 106, 119-120.

It is suggested that a purchaser (such as Cohen) should have no right against a receiver because otherwise the purchaser would acquire a windfall, since, he like the seller, knew nothing of that right when he purchased. But in a great variety of instances, purchasers are permitted to acquire windfalls, e.g., a buyer of land on which oil is discovered after the sale. The *Restatement of Contracts*, § 171(2) reads: "Unless otherwise provided in the assignment or by agreement of the assignee with the assignor or with the obligor, an assignee under an effective assignment for value has the same right to any securities for the assigned right that were available to the assignor, though he has not bargained for them, as if the assignor had agreed to transfer them." [42] If Glass was guilty of wrongdoing, that Cohen's estate will unexpectedly benefit can work no harm to Glass. We therefore reject the New York rule and apply the rule adopted elsewhere.[42a]

Accordingly, we hold that appellants have the right, for their own benefit and that of other holders of non-deposited bonds,[42b] to have Glass surcharged on account of his wrongdoing, if any. In so holding, we do not mean that, even if appellant lacked that right, the district court should have disregarded the merits of appellants' charges against Glass

[42] See Williston, *Contracts* (Rev. ed. 1936) § 447A.
And so where the assignee is ignorant thereof at the time of the assignment; see, e.g., *Gay* v. *Hudson River Electric Power Co.*, 180 F. 222, 227; *Edwards* v. *Bay State Gas Co.*, 184 Fed. 979, 982.

[42a] See, e.g., cases cited in note 38, *supra*.

[42b] See note 13, *supra*.

BLEED THROUGH POOR COPY

and should have refrained from directing an investigation for the benefit of whatever persons may have been injured by Glass' alleged misconduct. It is fortunate, however, that appellants have the requisite standing and self-interest in the investigation, since it might well be difficult for the court otherwise to obtain the needed services of a lawyer and an expert accountant.[43]

6. Appellants contend that the New Middle States company should be held liable together with the receivers. On oral argument appellants supported this contention by reference to an agreement made by the new company, in connection with the reorganization, to discharge the receivers' obligations. Appellees did not, on the oral argument, question the existence of such an agreement; but we have not found it in the record before us. If there is one, we think it would not include the kind of liability here sought to be imposed, absent fairly specific language indicating otherwise. We leave that question for the court below.

Should it, however, appear (of course, we do not know that it will) when all the facts are before the court, that the reorganization committee and, through it, the new company, conspired with Glass to deprive non-depositing United bondholders of their legitimate share of the United assets[44] in a way which involved a fraud on the court,[45] then it may be that, notwithstanding the decrees, the new company will be liable with the receivers. *Jackson* v. *Smith*, *supra*; *Ferguson* v. *Wachs*, 96 F. (2d) 910 (C. C. A. 7); cf. *Irving Trust Company* v. *Deutsch*, 73 F. (2d) 121, 123, 125 (C. C. A. 2).

---

[43] For the court merely to appoint a lawyer who would be paid on a contingent basis and who (unlike appellants' lawyer, who may in any event look to the Cohen estate for payment) would go unpaid if unsuccessful, would be insufficient; the services of an expert accountant are also needed. The S. E. C. is not authorized by statute to engage in such an undertaking except under the Chandler Act.

[44] We do not here refer to the doctrine of the *Boyd* case.

[45] Cf. *Hazel-Atlas Co.* v. *Hartford Co.*, 322 U. S. 238.

7. We think that undoubtedly, in connection with the receivers' final accounting and discharge, appellants should have access to the engineer's and accountants' reports and, indeed, to anything in the books and papers in the hands of the receivers. Since, as Glass had made clear, the affairs of the various companies in the several receiverships were "administered as a unity," and were "inextricably intertwined," there is every reason why appellants in connection with the United receivership, should have similar access to the receivers' books, records and files in all the receiverships in the court below.[46] Appellees argue that the final accounting in each receivership should stand on its own bottom. But it would seem from Glass' statement that such a method would be highly artificial and might unduly complicate matters, since facts revealed with respect to one receivership might so affect another as to necessitate undesirably the reopening of an order of discharge theretofore made. We think orderly administration requires that the final accountings and discharges should be dealt with just as the court dealt with the receiverships when they were active, i.e., as a unit.

REVERSED AND REMANDED

[46] Appellees contend that the examination which appellants ask concerns the value of the physical properties; that the physical properties were in the custody of ancillary receivers in other jurisdictions; and that, as those ancillary receivers have been discharged, it will be improper to permit such examinations. But, as the receivers' interim reports and Glass' affidavits show, the ancillary receivers reported to the receivers in the court below. These receivers reported on June 1925 that they "have conducted a principal office with which the ancillary receivers have been in constant touch by daily correspondence, telephone and telegraph concerning day to day developments, sale and storage of oil, drilling of wells and other affairs, in connection with the running of the business." More important, appellants seek no relief with respect to the physical properties but want, and should be allowed, access to data concerning those properties since such data may have an important bearing on the questions involved here.

BLEED THROUGH POOR COPY

SWAN, *Circuit Judge* (dissenting):

These are appeals from two orders in an equity receivership. One of the orders approved the final report and accounting of the receivers of United Oil Producers Corporation and discharged the receivers in respect of all matters embraced in their said report and accounting; the other order denied a motion for a discovery and inspection of the books of account and other papers of the receivership. The appellants are the executors of William W. Cohen, deceased, and his widow, sole beneficiary under his will. Any rights they may have to surcharge the receivers or to inspect the books and papers of the receivership are derived under the will by reason of Cohen's ownership of $32,200 of bonds issued by United. Unless Cohen at the time of his death in 1940 had rights against the receivers based on their conduct as such receivers, the appellants have no standing to object to the final accounting. It was imperative, therefore, for them to prove that Cohen did have such rights. In my opinion they failed to make such proof. Consequently the orders should be affirmed.

The theory upon which the appellants assert a right to object to the receivers' accounting is that they were guilty of a breach of fiduciary duty in not reporting to United's bondholders and to the district court that United's assets were of sufficient value to pay the bonds in full and in consequence of the concealment of such information the assets were sold at judicial sales in 1929 at too low a price. Such concealment is said to be equivalent to a fraudulent misrepresentation as to the value of United's bonds and to have caused the bondholders who elected to take cash instead of new securities under the plan of reorganization, to accept only 68 cents on the dollar instead of getting full payment of their bonds. Assuming these allegations to be true, the receivers' misrepresentation was a breach of duty to the owners of bonds at the time when the misrepresentation was made, that is, at a time prior to the judicial sales.

The $32,200 of bonds upon which Cohen received 68 cents on the dollar were acquired by him at some unspecified date after the judicial sales. Hence the receivers' misrepresentations as to their value were not a tort against Cohen but against the owner of the bonds in November 1929. In *Elias* v. *Clarke*, 143 F. 2d 640, 644 (C. C. A. 2) we held that under New York law a claim for fraud or misrepresentation in connection with an obligation evidencing a debt, whether for damages or rescission, does not pass with the transfer of the obligation in the absence of a special assignment of the claim. Cohen was a securities broker in New York City and it is a natural inference that he purchased the bonds here. If so, neither he nor his executors acquired any right to claim damages for the receivers' tort to his predecessor in title.[1] If he acquired them outside the State of New York and in a state where the seller's tort claim would pass without a special assignment of the claim, it devolved upon his executors to make proof of that fact in order to show their right to object to the receivers' final accounting. They offered no such proof. The district court held that they were "without standing to object to the final report and accounting." This conclusion was right, whether or not we agree with the reasoning by which the district judge reached it. Accordingly I think the orders should be affirmed.

[1] The majority opinion suggests that because this is a federal receivership we may hold that Cohen's purchase of the bonds, even if the transfer occurred in New York, passed to him the seller's tort claim against the receivers. This seems to me in direct conflict with the rule of *Erie* v. *Tompkins*.

BLEED THROUGH POOR COPY

(REPORTED 156 FED. (2) 697)

UNITED STATES CIRCUIT COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 314—October Term, 1945.

(Argued June 11, 1946 Decided July 9, 1946.)

Docket No. 20275

JOSEPH A. PHELAN,

Complainant,

v.

MIDDLE STATES OIL CORPORATION, *et al.,*

Defendants.

SOPHIE D. COHEN, individually and as Executrix, and MEYER KRAUSHAAR and CLARENCE CONE, as Executors of the Last Will and Testament of William W. Cohen, deceased,

Appellants,

v.

JOSEPH P. TUMULTY and JOSEPH GLASS, as Receivers of United Oil Producers Corporation, *et al.*, and MIDDLE STATES PETROLEUM CORPORATION,

Appellees.

Before:

L. HAND, SWAN and FRANK,

Circuit Judges.

Appeal from the District Court of the United States for the Southern District of New York.

From an order entered on the mandate of this court, the executors of the will of William W. Cohen, deceased, and Sophie D. Cohen, individually, appeal.

MEYER KRAUSHAAR, *for appellants.*
LESLIE KIRSCH, *for appellees.*

PER CURIAM:

This is an appeal from the order entered on the mandate of this court in a prior appeal entitled *Phelan* v. *Middle States Oil Corp.*, 154 F. 2d 978. In addition, the appellants have moved that our mandate be recalled and modified, or be construed in the manner they desire; while the appellees hav moved to dismiss the appeal. Without reciting the terms of the order it will suffice to say that it fully conforms to our mandate. The opinion on the former appeal did not order a reference to a special master. Rule 53(b) of the Federal Rules of Civil Procedure, 28 USCA following § 723(c) declares that a reference to a master is the exception, not the rule. Whether in a given case a reference should be ordered is a matter primarily within the discretion of the district judge. He has not as yet exercised his discretion and the order on appeal leaves him free to do so hereafter. Nor does the order, as the appellants assert, unduly restrict their investigation. It grants them inspection of "all books, papers, documents, balance sheets, appraisals and inventories in the hands of the Receivers of any of the companies heretofore or now in receivership in this cause." If it shall appear to the district court that examination of the books of the new company is essential to show values as of the time of the judicial sales, we cannot assume that such examination will be denied. The appellants' complaint on this score is premature. Both motions are denied and the order appealed from is affirmed.

BLEED THROUGH POOR COPY

Statutes Involved.

Civil Practice Act of the State of New York, Article 2, §§ 24, 48 Subdivision 5, and 53:

§ 24. Effect of stay of commencement of action.

Where the commencement of an action has been stayed by injunction or other order of a court or judge or by statutory prohibition, the time of the continuance of the stay is not a part of the time limited for the commencement of the action.

§ 48. Actions to be commenced within six years.

The following actions must be commenced within six years after the cause of action has accrued:

* * * * * *

5. An action to procure a judgment on the ground of fraud. The cause of action in such a case is not deemed to have accrued until the discovery by the plaintiff, or the person under whom he claims, of the facts constituting the fraud.

* * * * * *

§ 53. Limitation where none specially prescribed.

An action, the limitation of which, is not specifically prescribed in this article, must be commenced within ten years after the cause of action accrues.

Judgment Appealed From.

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

At a Stated Term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Courthouse in the City of New York, on the 11th day of January, one thousand nine hundred and fifty-five.

Present:

HON. LEARNED HAND,
HON. THOMAS W. SWAN,
HON. JEROME N. FRANK,
Circuit Judges.

JOSEPH A. PHELAN,
Complainant,

v.

MIDDLE STATES OIL CORPORATION, et al.,
Defendants.

Appeal from the United States District Court for the Southern District of New York.

This cause came on to be heard on the transcript of record from the United States District Court for the Southern District of New York, and was argued by counsel.

ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged, and decreed that the judgment of said District Court be and it hereby is affirmed.

It is further ordered that a Mandate issue to the said District Court in accordance with this decree.

/s/ A. DANIEL FUSARO,
Clerk.